Supreme Court, U.S.
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In the

Supreme Court of the United States

NATIONAL FIRE INSURANCE
COMPANY OF HARTFORD,

Petitioner,

v.

FORTUNE CONSTRUCTION COMPANY,

Respondent.

Petition for a Writ of Certiorari to the
United States Court of Appeals for the Eleventh Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

If a performance bond incorporates by reference the underlying contract, but does not specify on its face that the surety is responsible for delay damages arising from untimely performance of the underlying contract, is the surety liable for consequential delay damages?

PARTIES TO THE PROCEEDINGS AND CORPORATE DISCLOSURE STATEMENT

The caption of this petition contains the names of all of the parties to the proceeding in the court whose judgment is sought to be reviewed.

CORPORATE DISCLOSURE STATEMENT

National Fire Insurance Company of Hartford is a wholly owned subsidiary of CNA Financial Corporation.

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OPINIONS BELOW

The February 7, 2003 opinion of the Eleventh Circuit Court of Appeals, the judgment of which is sought in this petition to be reviewed, is reported at 320 F.3d 1260, and is reprinted in the Appendix to this petition at pp. 1-38. The prior judgment of the United States District Court for the Southern District of Florida was entered on July 23, 2001 in case no. 97-22439 Civ-King. It is unpublished, and is reprinted in the Appendix at pp. 39-40. The underlying trial court order relevant to the question presented by this petition is the July 10, 1998, Order Granting Plaintiff's Motion for Partial Summary Judgment. It is reprinted in the Appendix at pp. 41-42.

STATEMENT OF JURISDICTION

The judgment of the Eleventh Circuit Court of Appeals was entered on February 7, 2003. A timely petition for rehearing was denied on April 1, 2003 (Appendix, pp. 43-44). The jurisdiction of the Court is invoked under 28 U.S.C.A. 1254(1).

CONSTITUTIONAL PROVISIONS, TREATIES, STATUTES, RULES, AND REGULATIONS

No constitutional provisions, treaties, statutes, rules or regulations are relevant to this petition.

STATEMENT OF THE CASE

Arkin Construction Company, Inc. ("Arkin") was a subcontractor to Fortune Construction Company ("Fortune") for the construction of two apartment complexes known as West Brickell and Winston Park.

The subcontracts included deadlines for Arkin to complete its work, and set forth sums to constitute liquidated delay damages in the event of untimely performance. National Fire Insurance Company of Hartford ("National Fire") issued payment and performance bonds on behalf of Arkin for both projects.

Arkin failed to pay its subcontractors and suppliers funds due in excess of one and a half million dollars for work performed on the two projects. Pursuant to its payment bond obligations, National Fire paid the subcontractors and suppliers. Arkin also failed to complete the projects by their original deadlines. Arkin continued to work on the projects after the original deadlines had passed, until it eventually ceased work entirely. Fortune declared Arkin to be in default of the construction subcontracts about two weeks later. At that time, the balance of the subcontracts that had yet to be paid to Arkin was in excess of two and a half million dollars.[1] However, the cost to complete Arkin's unfinished work was substantially less than two and a half million dollars.

The primary dispute that led to this litigation was a difference of opinion between National Fire and Fortune as to which had a superior right to the unpaid portion of Arkin's subcontracts that would remain after the completion of Arkin's work (the "contract balances"). National Fire asserted that, by virtue of its payments to payment bond claimants, it possessed

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[1]The Winston Park subcontract price, adjusted for change orders, was $10,899.975. Arkin was paid $8,709,728.80 for work performed prior to the declaration of default. Thus, the "Winston Park contract balance" was $2,190,246.20. The West Brickell subcontract price, adjusted for change orders, was $4,740,754.39. Arkin was paid $4,304,627.55 for work performed prior to the declaration of default. Thus, the "West Brickell contract balance" was $435,126.84.

equitable subrogation rights to the contract balances. Fortune contended that it had a superior right to apply those same contract balances to its claims against Arkin that arose prior to default; the most significant of which was liquidated delay damages on the West Brickell project that were well in excess of one and a half million dollars on the date of default.

National Fire brought the underlying action in the United States District Court for the Southern District of Florida to require Fortune to pay National Fire the contract balances that remained after the completion of Arkin's work. Fortune defended by asserting that it had a superior right to the contract balances, and filed a counterclaim asserting that National Fire had breached its performance bond obligations. The basis for jurisdiction was diversity, pursuant to 28 U.S.C. §1332.

The District Court Order that is relevant to this petition arose from National Fire's First Motion for Partial Summary Judgment, which was subtitled "Payment Bond Equitable Subrogation" (Appendix pp. 51-66). National Fire argued that under the doctrine of equitable subrogation, it had a superior right to recover the sums it paid to payment bond claimants from the contract balances. The District Court, Judge James Lawrence King, resolved this issue in its Order Granting Plaintiff's Motion for Partial Summary Judgment (Appendix pp. 41-42), wherein it concluded that "[t]he Court finds that Plaintiff has a right to recoup payments it made under the payment and performance bonds from the unpaid balance of the subcontract, this right being superior to Defendant's right to apply that balance to claims it may have against the defaulting subcontractor."

The case proceeded to a jury trial that was largely an accounting exercise to determine the precise cost to complete Arkin's work and the resultant contract

balances. The Court instructed the jury that it had found as a matter of law that National Fire had a right to recoup payments it made under the payment bonds from the contract balances, and that this right was superior to Fortune's right to apply the contract balances to claims that it might have against Arkin, including its claims for liquidated delay damages. The jury verdict determined that the remaining contract balances after the completion of Arkin's work were $336,896.28 for the Winston Park project and $255,774.00 for the West Brickell project, to which the District Court added pre-judgment interest in its final judgment (Appendix, pp. 39-40).

Fortune appealed seven issues to the Eleventh Circuit, of which only one is relevant to this Petition: whether the District Court erred in granting summary judgment for National Fire as to Fortune's claim for set-off of the liquidated delay damages against the subcontract balances. The Eleventh Circuit properly affirmed the District Court's grant of summary judgment in favor of National Fire on this issue as follows:

> A performing payment bond surety stands in the shoes of the laborers and materialmen who might have had liens on the property. That right is generally superior to the rights of either the principal or the obligee. To the extent of the payment bond claims actually and properly paid, National Fire's right to any unpaid contract balances is superior to Fortune's liquidated delay damages claim.

(Appendix p. 24). Unfortunately, the Statement of the Case does not end here.

The Eleventh Circuit opinion is dominated by its

consideration of two issues that were not before the Court. First, the Eleventh Circuit mistakenly believed that National Fire sought to assert equitable subrogation rights arising from the performance bonds, rather than the payment bonds, and held that the District Court erred by granting National Fire summary judgment on equitable subrogation arising out of the performance bonds. However, no such claim was made by National Fire, nor would there be any basis for such a claim, and no such summary judgment motion was made or granted.

With the benefit of hindsight, the District Court's Order Granting Plaintiff's Motion for Partial Summary Judgment could have been more artfully worded, as the phrase "payments it made under the payment and performance bonds" apparently confused the Eleventh Circuit. It did not confuse any of the parties to the District Court action, because National Fire did not claim or assert any rights to equitable subrogation arising from the performance bonds.[2] As National Fire did not pay any money due to the performance bonds, there would be no money to recover. This was a non-issue before the District Court and was not raised by Fortune or National Fire in their briefs to the Eleventh Circuit.

Next, the Eleventh Circuit mistakenly believed

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[2]The motion for summary judgment was entitled "National Fire's First Motion for Partial Summary Judgment (Payment Bond Equitable Subrogation)." Paragraph four of the motion states:

> This motion is based upon, and limited to, the rights and obligations arising from the two payment bonds. It is not intended to touch upon issues related to the two performance bonds. This motion is solely intended to resolve legal disputes regarding rights and obligations under the payment bonds.

Appendix, p. 53.

that Fortune sought to recover the liquidated delay damages from National Fire in the underlying suit under a theory that they were a responsibility of National Fire under the performance bonds. Such a theory of recovery was not pled or otherwise asserted by Fortune before the District Court, likely because it was expressly barred by the Florida Supreme Court's holding in *American Home Assurance Co. v. Larkin General Hospital, Ltd.*, 593 So. 2d 195 (Fla. 1992) which was properly interpreted and followed by the Fifth Circuit Court of Appeals, applying Florida law, in *L & A Contracting Co. v. Southern Concrete Services, Inc.*, 17 F.3d 106 (5th Cir. 1994). Under the holding of these cases, if a performance bond specifies that it incorporates the underlying contract, but it does not specify on its face that the surety is responsible for delay damages arising from untimely performance of the underlying contract, liability for delay damages is not imposed upon the surety. To attempt to avoid the holding of *Larkin General Hospital*, Fortune framed its theory of recovery of delay damages as a "set-off" that could be applied to Arkin's unpaid contract balances, rather than an affirmative claim for recovery of damages under the performance bonds. While the Eleventh Circuit correctly held that National Fire's equitable subrogation rights arising from its payment bonds were superior to Fortune's right to set-off its delay claim against Arkin, the Eleventh Circuit mistakenly went a step further and addressed a performance bond theory of recovery that was not even asserted by Fortune before the District Court, and is entirely absent from Fortune's pleadings.

As the Eleventh Circuit's opinion is largely devoted to its misunderstanding of the record, it did not have the benefit of briefs on issues that were not part of the case. An apparent consequence is that the Eleventh

Circuit did not appreciate that the relevant language of the performance bonds issued by National Fire is the same as the language of the performance bonds considered by the Florida Supreme Court in *Larkin General Hospital* and the Fifth Circuit in *L & A Contracting*. As a result, the Eleventh Circuit issued an opinion that interprets commonly used performance bond form language to create liability for delay damages, although this is in direct conflict with the Florida Supreme Court's consideration of the same bond form language in *Larkin General Hospital*, as well as the Fifth Circuit's interpretation and application of that case in *L & A Contracting*.

REASONS FOR GRANTING THE WRIT

I. INTRODUCTION.

The opinion of the United States Court of Appeals for the Eleventh Circuit should be reviewed by this Court for several reasons. First, it directly conflicts with an opinion of the Fifth Circuit on the same important matter. Second, the Eleventh Circuit has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's supervisory power. Due to its misunderstanding of the issues before the District Court, the Eleventh Circuit's opinion largely addresses matters that were not part of the case. Without the benefit of appropriate briefs on such extraneous matters, the Eleventh Circuit was unaware of the conflict and forum shopping that its opinion would create.

This case has exceptional importance beyond the parties' particular dispute, as an unintended consequence of the Eleventh Circuit's opinion will be to exponentially increase the liability of sureties under

presently outstanding bonds. In short, the Eleventh Circuit has accidentally imposed an opposite interpretation than the Florida Supreme Court on the question of whether widely used standard form language operates to impose liability upon a surety for delay damages. In so doing, the Eleventh Circuit also created a conflict with the Fifth Circuit, which had previously correctly interpreted the Florida Supreme Court's opinion.

The granting of a petition for certiorari is an act of grace. *Stone v. Powell*, 428 U.S. 465 (1976). We submit that such grace is warranted here to protect the surety industry from the drastic unintended consequences that would be suffered as a result of the Eleventh Circuit's error.

II. DISCUSSION OF CONFLICT, DEPARTURE, AND CONSEQUENCES.

It is highly unusual for two Circuits of the United States Courts of Appeals to have diametrically conflicting interpretations of a state Supreme Court opinion. That is the case here. In *American Home Assurance Co. v. Larkin*, 593 So. 2d 195 (Fla. 1992), the Court stated the issue and holding as follows:

> The issue is whether a surety on a performance bond can be held liable for consequential delay damages caused by the contractor's default. We hold that a surety cannot be held liable for delay damages due to the contractor's default unless the bond specifically provides coverage for delay damages.

Larkin General Hospital, 593 So. 2d at 196. The Fifth

Circuit, in *L & A Contracting Co. v. Southern Concrete Services*, 17 F.3d 106 (5th Cir. 1994), expressed that *Larkin General Hospital* required the face of the bond itself to express liability for delay damages:

> *Larkin* plainly states that the express terms of the bond provide the sole measure of [the surety's] obligation. If [the surety's] liability for delay damages is not "*expressed in the bond*", *id.* at 198 (emphasis added, internal quotation omitted), [the surety] has no such liability.

L & A Contracting, 17 F.3d at 112. However, the Eleventh Circuit has now reached the opposite conclusion:

> *Larkin General Hospital* could possibly be interpreted to mean that a performance bond surety cannot be held liable for, or denied subrogation for, delay damages, whether liquidated or unliquidated, unless the responsibility for delay damages is specified on the face of the performance bond. However, we do not read the decision that broadly.

Fortune Construction, 320 F.3d at 1275. The Eleventh Circuit opinion does not recognize its conflict with the Fifth Circuit. In all likelihood, the Eleventh Circuit did not realize that it was creating a conflict by holding that a surety may be liable for delay damages where the bond itself does not specifically so provide.[3]

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[3]The Eleventh Circuit's Opinion also does not suggest that it considered any of the progeny of *Larkin General Hospital*, such progeny is consistent with the Fifth District's interpretation. *E.g.*,

This conflict was an accidental byproduct of the Eleventh Circuit's misunderstanding of the claims addressed by the District Court. If the Eleventh Circuit had limited its consideration to issues that were before the District Court, no conflict would have been created. A grant of certiorari is only more appropriate where it is apparent that the conflict did not arise from a thoughtful and reasoned analysis, but from a misunderstanding of the record and issues, in a context where the conflict will have unintended consequences beyond the particular parties' dispute.

It is readily apparent that the Fifth Circuit's interpretation of *Larkin General Hospital* is correct, and the distinguishing factor relied upon by the Eleventh Circuit to support its interpretation and to distinguish *Larkin General Hospital* is wrong. The Eleventh Circuit believed that the performance bonds at issue in the instant case differed from the performance bond in *Larkin General Hospital* because "unlike the performance bond in *Larkin General Hospital*, the bonds at issue in this case expressly incorporated the subcontracts." (Appendix, p.22). This is the only basis asserted in the opinion to support the failure to follow the holding of *Larkin General Hospital* that a performance bond surety is not liable for delay damages unless the bond specifically provides coverage for delay damages, and it is just wrong. However, the bond in *Larkin General Hospital* contained the exact same form language incorporating the construction contracts as the bonds in the instant case.[4]

Federal Insurance Co. v. Southwest Florida Retirement Center, Inc., 707 So. 2d 1119 (Fla. 1998) and *Auto Owners Insurance Company v. Travelers Casualty & Surety Co.*, 227 F.Supp.2d 1248 (M.D. Fla. 2002).

[4]The opinion in *Larkin General Hospital* states that "[t]he language of the performance bond in the case at bar is identical to

Moreover, the "incorporation" distinction that is the basis of the Eleventh Circuit's opinion was expressly rejected in *Larkin General Hospital.* That case reached the Florida Supreme Court based upon a certification of conflict between *Arbor Club of Boca Raton, Inc. v. Omega Constr. Co.*, 565 So. 2d 357 (Fla. 4th DCA 1990) and *United States Fidelity & Guar. Co. v. Gulf Florida Dev. Corp.*, 365 So. 2d 748 (Fla. 1st DCA 1978). All of these cases, as well as the instant case, involved performance bonds that incorporated the underlying contracts, but did not specify on their face that the surety was responsible for delay damages.[5] The basis of the holding in *Arbor Club* was the same as the Eleventh Circuit's analysis in the instant case, that "the bond incorporated the construction contract by reference, and that contract provided for timely performance." *Arbor Club*, 565 So. 2d at 360. Thus, the *Arbor Club* court held the performance bond surety liable for delay damages. In conflict with *Arbor Club*, the court in *Gulf Florida*, faced with the same language in another performance bond, concluded that the terms of the performance bond limited the liability of the surety to the costs of completion and the costs of curing defective work. *Larkin General Hospital*, 593 So. 2d at 197. The Florida Supreme Court expressly adopted the holding of *Gulf Florida* and rejected the incorporation analysis of *Arbor Club. Larkin General Hospital*, 593 So. 2d at 198.

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the language in the performance bond in *Arbor Club, Inc. v. Omega Constr. Co.*, 565 So. 2d 357 (Fla. 4th DCA 1990) and *Gulf Florida.*" *Larkin General Hospital*, 593 So. 2d at 197. The opinion in *Arbor Club* did set forth the text of the bond in full, and it is the same as the bond language in the instant case. *Arbor Club*, 565 So. 2d at 359. The *Arbor Club* opinion even made specific note of the fact that the bond incorporated the contracts. *Arbor Club*, 565 So. 2d at 359 ("The bond also provides that the contract between Omega and Arbor 'is by reference made a part hereof.'").

[5] *See*, footnote 4.

In other words, without the benefit of appropriate briefs on a theory of recovery that was not addressed by the District Court, and due to the mistaken distinction that the bond in *Larkin General Hospital* did not incorporate the contract, the Eleventh Circuit erroneously reached the same interpretation and holding that was previously rejected by the Florida Supreme Court.

The Eleventh Circuit also apparently did not consider the more recent Florida Supreme Court case of *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998), which expressly reaffirmed that the proper interpretation of *Larkin General Hospital* is that the liability of a performance bond surety may not be extended by "contractual incorporation." *Southwest Florida*, 707 So. 2d at 1120. Specifically, the *Southwest Florida* opinion held that the "incorporation" analysis improperly "extends the liability on the bond by implication beyond the terms of the bond contract. This additional burden is in derogation of the analysis provided by *Larkin General Hospital*." *Id.* at 1120-1121. Thus, following *Southwest Florida*, it is beyond doubt that the Florida Supreme Court does not agree with the "incorporation" analysis relied upon in the Eleventh Circuit's Opinion.

The most recent reported decision to interpret *Larkin General Hospital* is *Auto Owners Insurance Company v. Travelers Casualty & Surety Co.*, 227 F.Supp.2d 1248 (M.D. Fla. 2002). As this decision is dated September 12, 2002, it presumably also was not considered by the Eleventh Circuit. The Middle District undertook an extensive evaluation and discussion of both *Larkin General Hospital* and the subsequent Supreme Court opinion in *Southwest Florida*. *Auto Owners*, 227 F.Supp.2d at 1264-1265. The *Auto Owners* opinion explains that, in *Southwest Florida*, the Florida

Supreme Court expressly "rejected the owner's argument that a surety's liability is co-extensive with the general contractor based on incorporation of the general contract into the performance bond." *Id.* at 1265. Similarly, the *Auto Owners* court found that "[a] holding that the incorporation provision may enlarge a surety's obligation under a bond, for both costs to complete a project and for damages that result from the project, would seem contrary to *Larkin*." *Id.*

While the Middle District reached the correct result in *Auto Owners*, unless the Eleventh Circuit's opinion is redressed, future litigants in that court will suffer a different result. The District Courts of the Eleventh Circuit are now bound to follow the Eleventh Circuit's interpretation of this same bond language as including liability for delay damages. *See*, *United States v. Lehder-Rivas*, 827 F.2d 682 (11th Cir. 1987). At the same time, the opposite result will be reached in a state court that is bound to follow *Larkin General Hospital*, rather than the Eleventh Circuit. Liability for delay damages under standard form performance bonds will turn on whether the action is in a state or federal court. A grant of certiorari is particularly appropriate in this circumstance, as further litigation in the lower courts cannot resolve this issue, but will only deepen the conflict and inconsistent results in an area of law where uniformity and predictability are prime virtues.

An irony is that even Fortune did not assert a claim for delay damages under the performance bonds in the District Court. Fortune framed its theory of recovery of delay damages as a "set-off" of claims against Arkin's contract balances, rather than an affirmative claim for recovery of damages under the performance bonds. Fortune also claimed entitlement to *post*-default delay damages arising after Arkin left the project from National Fire's alleged failure to satisfy

performance bond obligations in a more timely manner. However, nowhere in Fortune's Counterclaim, or anywhere else in the District Court record, did Fortune advance the theory that it was entitled to recover the pre-default delay damages from the surety because they are recoverable damages under the performance bond. It is a departure from the appropriate course of judicial proceedings for a Court of Appeals to so address matters not considered by the District Court. *See, Moses H. Cohn Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 28 and 35 (1983)("Ordinarily, we would not expect the Court of Appeals to pass on issues not decided in the District Court" although an exception may exist where special exceptions are at stake and there is no prejudice; dissent expressed that "I am disturbed, however, that the Court has sanctioned an extraordinary departure from the usual and accepted course of judicial proceedings by affirming the Court of Appeals decision on an issue that was not decided in the District Court."); *Singleton v. Wulff*, 428 U.S. 106 (1976)(general rule is that federal appellate court should not consider an issue not passed on below); *In re Beaty*, 268 B.R. 839 (9th Cir. 2001)(rejecting an assertion that a court ruling departed from the accepted and usual course of judicial proceedings because the record showed that the court had not failed to provide an opportunity to consider arguments on the issue).

The Eleventh Circuit's error threatens to accidentally devastate the surety industry.[6] The

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[6]While it is not generally the function of the United States Supreme Court to correct a misapplication of state law, exceptions have been recognized in this context. For example, in *Thomas v. American Home Products, Inc.*, 519 U.S. 913 (1996), it was recognized that such review could be appropriate "in exceptional cases with importance beyond the parties' particular dispute." *Thomas*, 519 U.S. at 916-917 (in dissent). An example of such an

Eleventh Circuit did not appreciate that the bond form language under consideration is presently in widespread use, nor did the Eleventh Circuit appreciate that this specific bond language had already been conclusively determined by the Florida Supreme Court and the Fifth Circuit to exclude surety responsibility for delay damages.[7] In fact, a multitude of bonds have been

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exceptional case is *Steele v. General Mills, Inc.*, 329 U.S. 433 (1947), where the Court's review was prompted by concern of the effect of the judgment below on the shipping industry in Texas. Another example is *Leavitt v. Jane L.*, 518 U.S. 137, 144-145 (1996), where the majority staunchly defended the practice of granting certiorari solely to review application of state law in an appropriate "exceptional case," expressing that the Court "undoubtedly should do so where the alternative is allowing blatant federal-court nullification of state law." The Court in *Leavitt* discussed *Wichita Royalto Co. v. City Nat. Bank of Wichita Falls*, 306 U.S. 103 (1939), where the only question was whether the Fifth Circuit Court of Appeals correctly followed principles of law contained in an opinion of the Supreme Court of Texas. *Leavitt*, 518 U.S. at 144. Analogous concerns for the surety industry in Florida arise in the instant case.

[7]The consequences of the Eleventh Circuit's error are exacerbated by the long established practice of the construction industry to use standard bond forms for the issuance of performance bonds. *See*, P. Bruner, et.al. *The Surety's Response to the Obligee's Declaration of Default and Termination* 17-Jan Construction Law 3 (ABA 1997). Until now, the use of standard bond forms has generally led to greater consistency and certainty in judicial construction, as courts and commentators frequently refer to the bond form under consideration. *See*, for example, 4 *Bruner & O'Connor Construction Law* §12:35 ("In *L & A Contracting Company v. Southern Concrete Services, Inc.* an obligee under an AIA Document A311-1970 performance bond. . ."). While there are various sources of bond forms, the Eleventh Circuit's opinion implicates the most commonly used bond form in the country today, which is known as AIA Document A311. *See*, 3 *Bruner & O'Connor Construction Law* § 8:156 (2003); A. Frakes, *Surety Bad Faith* 2002 U.Ill.L.Rev. 497 (2002). This form is promulgated by the American Institute of Architects, which has been involved in

issued under the belief and intention that this bond language does not include liability for delay damages. The Eleventh Circuit's opinion will serve to undercut the generally accepted rule that an interpretation placed upon a contract by the highest court of the state should not be affected by subsequent decisions. *See*, *City of Los Angeles v. Los Angeles City Water Company*, 177 U.S. 558 (1900). This principal is particularly applicable to the interpretation of an insurance policy or bond form that is in widespread use, as underwriting decisions are sensibly made in reliance upon germaine court decisions. *See*, *Farber v. Perkiomen Mut. Ins. Co.*, 88 A.2d 776 (Penn. 1952). Thus, when the proper construction of such language has been determined and established by a prior decision of a state Supreme Court, it may be expected that there will be future reliance upon such construction, and it is especially inappropriate to materially alter an established interpretation. *See*, *Id.* at 779. That is what has happened here. Unless redressed, the Eleventh Circuit's opinion will have the unintended result of exponentially increasing the liability of sureties under presently outstanding bonds, as long as the obligee is successful in the forum shopping that is invited by this incongruity. Simply stated, the liability of a surety for delay damages will turn upon whether the action is brought in a state or Federal court.

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authoring industry standard forms for well over a century. 2 *Bruner & O'Connor Construction Law* § 5:12 AIA Standard Forms (2003). While the AIA also promulgates other bond forms, the A311 form is perceived in the industry to be the most even-handed, and therefore is the most frequently used. *Id.* Variants of this same form were addressed in *L & A Construction*, *Larkin General Hospital*, *Arbor Club*, *Gulf Florida*, *Auto Owners* and *Southwest Florida*. *See*, footnote 4.

III. CONCLUSION

The Eleventh Circuit has accidentally imposed an opposite interpretation than the Florida Supreme Court on whether the same standard form language operates to impose liability upon a surety for delay damages. In so doing, the Eleventh Circuit also created a conflict with the Fifth Circuit, which had previously correctly interpreted the Florida Supreme Court's opinion. Moreover, this error would not have occurred if the Eleventh Circuit had not departed from the usual course of judicial proceedings by issuing an opinion on a theory of recovery that was not asserted before the District Court. It would be difficult to overestimate the degree of liability impacted by the Eleventh Circuit's opinion in unrelated cases. This did not occur because the Eleventh Circuit intended to accomplish this result. Rather, it arose only because the Eleventh Circuit misinterpreted the proceedings before the District Court and erroneously believed that it was considering different bond language then considered by the Florida Supreme Court in *Larkin General Hospital* and the Fifth Circuit in *L & A Construction*. We submit that this is an exceptional case, warranting the grace of a grant of certiorari, and respectfully request that this petition for a writ of certiorari be granted.

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(Any footnotes trail end of each document)
No. 01-15124
U.S. 11th Circuit Court of Appeals

D.C. Docket No. 97-02439-CV-JLK

NATIONAL FIRE INSURANCE
COMPANY OF HARTFORD,
Plaintiff-Counter-
Defendant-Appellee,

versus

FORTUNE CONSTRUCTION COMPANY,
Defendant-Counter-
Claimant-Third-Party-
Plaintiff-Appellant,

ARKIN CONSTRUCTION COMPANY, INC.,
Third-Party-Defendant

Appeal from the United States District Court
for the Southern District of Florida

(February 7, 2003)

Before TJOFLAT and KRAVITCH, Circuit Judges, and VINSON*, District Judge.
VINSON, District Judge:

The primary issue presented by this appeal is whether a surety on construction contract performance and payment bonds issued on behalf of a subcontractor has superior rights to retained contract balances in the possession of the general contractor when the general contractor completed the performance and has unsatisfied claims against the defaulting subcontractor.

I. BACKGROUND

This case arises out of two construction projects - - - the Winston Park project in Coconut Creek, Florida, and the West Brickell project in Miami, Florida. As general contractor on the projects, Fortune Construction Company ("Fortune") entered into two separate subcontracts with Arkin Construction Company ("Arkin") to build the two apartment complexes, the Winston Park Subcontract and the West Brickell Subcontract. National Fire Insurance Company ("National Fire"), as surety, issued on behalf of Arkin, as principal, performance and payment bonds for the two construction projects. The performance bond and payment bond documents for the Winston Park project were standard forms issued by the American Institute of Architects. Fn1 The performance bond and payment bond documents for the West Brickell project were drafted by National Fire with language that materially differed from the Winston Park bonds. Each of the performance bonds and each of the payment bonds incorporated the appropriate subcontract between Fortune and Arkin by reference.

During construction of the two projects, Arkin began experiencing financial difficulty. National Fire provided financing to Arkin for a short time, but later refused to continue to finance Arkin. Both projects were behind schedule by this time. Arkin's financial difficulties prompted Fortune and National Fire to enter into negotiations about what to do when Arkin defaulted. There was some discussion about National Fire procuring a completion contractor and about the possibility that Fortune could complete construction. The West Brickell project was near completion, but a substantial amount of work still needed to be done on the Winston Park project. Negotiations were still

ongoing when, on May 29, 1997, Arkin abandoned both construction projects. On June 12, 1997, Fortune declared Arkin in default and notified National Fire accordingly.

A flurry of letters between the attorneys for Fortune and National Fire ensued. During this increasingly acrimonious exchange, National Fire contends that it tendered, or offered to tender, a completion contractor. While National Fire asserts that Fortune rejected this tender because Fortune wanted to complete construction itself, Fortune maintains that the tender was never made. Fortune demanded that National Fire perform its obligations under both performance bonds by completing the subcontracts. National Fire did not do so. While National Fire made payments to payment bond claimants on both projects, both of the construction projects were actually completed by Fortune as the general contractor, and Arkin is now a dissolved corporation.

The construction subcontracts between Fortune and Arkin each contained a clause obligating Arkin to pay liquidated damages for delays in completing the projects. The Winston Park Subcontract provided for liquidated damages of $35 per day per incomplete apartment and $1,000 per day for incomplete common areas. The West Brickell Subcontract provided for liquidated damages after a specified date of $30 per day per incomplete apartment. Due to Arkin's dilatory performance during the Winston Park and West Brickell construction, Fortune invoked these liquidated delay damages clauses before Arkin abandoned the projects. By the time Arkin defaulted, Arkin owed $1,693,500 in liquidated delay damages on the Winston Park project and $93,600 in liquidated delay damages on the West Brickell project. The subcontracts also made Arkin

responsible for the acts and omissions of its own sub-subcontractors. Allied Fire Protection Systems ("Allied"), one of Arkin's sub- subcontractors, failed to pay Davis-Bacon Act wages to its laborers for work performed on the West Brickell project, which apparently involved federally subsidized housing. Consequently, the Department of Labor jointly charged Fortune, Arkin, and Allied a total of $71,126 in back wages attributable to Allied's improper payments, which Fortune paid.

In addition to the West Brickell Subcontract between Fortune and Arkin, the parties entered into a letter agreement dated January 15, 1996 (the same date as the West Brickell Subcontract). This letter agreement recognized that the electrical work had been excluded from Arkin's subcontract on the West Brickell project, but that Arkin had full responsibility for cost overages if the cost of the electrical work exceeded $669,000. Arkin's responsibility was "either finding a replacement subcontractor" for the electrical work at $669,000 or "issuing a credit change order to Fortune" for any amount incurred over and above $669,000. Fn 2 However, this letter agreement was not listed as part of the contract documents in the West Brickell Subcontract, which contained two merger and integration clauses. During the West Brickell construction, Fortune's original electrical subcontractor, Monohan's Electric Co., defaulted and did not complete the electrical work. Arkin failed to provide another electrical contractor to complete the project within the fixed $669,000 price. In hiring another electrical contractor, Fortune incurred additional costs amounting to $404,118.81 in excess of $669,000, Fn 3 for which Fortune claims a credit against Arkin.

After Fortune completed the two construction projects, Fortune presented National Fire with an accounting of its "performance" costs to complete the Arkin subcontracts. National Fire then prepared an accounting of the net remaining contract proceeds. Fn4 According to National Fire, the remaining contract proceeds exceeded Fortune's costs of completion. National Fire requested that, according to the terms of the bonds, the unpaid contract balances be credited to the respective subcontracts and paid to National Fire, as the subrogee of Arkin. Fortune refused to pay National Fire the contract balances, claiming that it had superior right to the contract balances due to National Fire's failure to perform on its performance bonds and because of Fortune's right to set off the remaining contract claims Fortune had against Arkin. National Fire initiated this civil action against Fortune alleging assignment of Arkin's rights under the subcontracts, equitable subrogation, and breach of the bond contracts. Fortune filed a counterclaim against National Fire for failure to perform under the performance bonds and failure to make the required payments under the payment bonds with respect to payments for Davis-Bacon Act violations, electrical overages, and the liquidated delay damages. Fortune also joined Arkin as a third party defendant responsible for the same damages, due to its breach of the two subcontracts.

Before trial, National Fire filed seven different motions for partial summary judgment. Fn 5 The district court entered three separate orders granting partial summary judgment with respect to several of National Fire's motions and granted the remainder in a pretrial conference order. In its first partial summary judgment order, the district court pointed to the language of the "Performance Bond Contract," although the court did not specify which performance bond, Fn 6 and held that

National Fire had a right to equitable subrogation "under the payment and performance bonds." Thus, the district court held that National Fire's equitable subrogation right to the contract balances was superior to Fortune's right to set off its claims against Arkin under both the payment and the performance bonds. In its pretrial conference order, the district court characterized this ruling as establishing that, to the extent the contract balances exceeded Fortune's reasonable costs to complete construction after Arkin's default, "the excess is to be paid to National Fire up to the amount of National Fire's payment bond expenditures." (R.67 at 2.) In that same order, the district court held that "National Fire had no obligation to complete [construction itself] or to tender [a completion contractor], but rather its obligation was to pay the excess of the costs to complete the contract over the contract balance, if any." Fn 7 (R.67 at 3.) According to the district court, as a matter of law, National Fire's failure to complete construction or to arrange for the completion of construction was not a breach of National Fire's performance bond obligations, and thus Fortune was not entitled to consequential damages from National Fire for the costs that Fortune incurred due to Arkin's default under the subject subcontracts.

In its second order granting National Fire partial summary judgment, the district court held that the letter agreement between Fortune and Arkin concerning liability for electrical overages was a separate agreement that had not been integrated into the contracts on which the bonds had been issued. In its third order granting National Fire partial summary judgment, the district court summarily dismissed with prejudice Fortune's Davis-Bacon wage claim against National Fire, without explanation.

At trial, the district court directed judgment as a matter of law in favor of Fortune on its third party claim against Arkin in the amount of $1,748,150 as to the Winston Park project and $432,000 as to the West Brickell project. These amounts included the Davis-Bacon wage claim, the electrical overage costs, and the liquidated delay damages. Fn 8 After this ruling, the only issues that remained for the jury at trial were: a determination of the reasonable costs Fortune incurred in completing construction, Fn 9 the amount of unpaid contract balances at the time of Arkin's default, and the amount of payment bond claims paid by National Fire. The district court instructed the jury to this effect, incorporating several of the court's prior rulings. Fn 10 The jury returned a verdict in favor of National Fire, finding that contract balances remained on both projects after the deduction of Fortune's reasonable costs to complete construction, Fn 11 and awarded National Fire $255,774 as to the West Brickell project and $336,896.28 as to the Winston Park project, to which the district court added prejudgment interest. This appeal followed.

II. STANDARD OF REVIEW

The standard of review for a district court's rulings on motions for summary judgment is de novo, and an appellate court is to apply the same legal standards that bound the district court. See Sarfati v. Wood Holly Assocs., 874 F.2d 1523, 1525 (11th Cir. 1989); Carlin Communication Inc. v. Southern Bell Tel. & Tel. Co., 802 F.2d 1352, 1356 (11th Cir. 1986). Likewise, de novo review is appropriate when addressing the construction of written contracts. See Securities & Exchange Comm'n v. Elliott, 953 F.2d 1560, 1582 (11th Cir. 1992). A jury's verdict is reviewed for sufficiency of the evidence and will not be overturned unless no rational trier of

fact could have reached the same conclusion based upon the evidence in the record. See Quick v. Peoples Bank of Cullman County, 993 F.2d 793, 798 (11th Cir. 1993).

A motion for summary judgment should be granted when "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(c). "[T]he plain language of Rule 56(c) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial." Celotex Corp. v. Catrett, 477 U.S. 317, 322,106, S. Ct. 2548, 2552, 91 L. Ed. 2d 265, 273 (1986); see also Morisky v. Broward County, 80 F.3d 445, 447 (11th Cir. 1996). On a summary judgment motion, the record and all reasonable inferences that can be drawn from it must be viewed in the light most favorable to the non-moving party. See Whatley v. CNA Ins. Cos., 189 F.3d 1310, 1313 (11th Cir. 1999).

We review a district court's grant of judgment as a

sufficient conflicts exist in the evidence to necessitate submitting the matter to the jury or whether the evidence is so weighted in favor of one side that one party must prevail as a matter of law." Thosteson v. United States, 304 F.3d 1312, 1316 (11th Cir. 2002). The evidence is evaluated in the light most favorable to the non-moving party. Id.

III. Discussion

A. Equitable Subrogation and Entitlement to Set-Off

The major issue raised in this appeal is National Fire's equitable subrogation rights under the two performance bonds and the two payment bonds. National Fire asserts that it possesses a superior right to the unpaid contract balances in light of a surety's recognized right to equitable subrogation. Fn 12 The District Court agreed and ruled below that National Fire had superior equitable subrogation rights under both its payment and its performance bonds. However, Fortune argues that the liquidated delay damages, Davis-Bacon Act violations, and the electrical overage costs incurred by Arkin should be set off against any unpaid contract balances that National Fire is claiming through equitable subrogation.

Fortune relies primarily upon United States v. Munsey Trust Co., 322 U.S. 234, 236, 67 S. Ct. 1599, 1600, 91 L. Ed. 2022, 2023 (1947), in which the Supreme Court of the United States addressed the issue of "whether percentages retained pursuant to contract by the United States may be subjected to its set-off claims despite the claims of a surety who has paid laborers and materialmen." In Munsey Trust, the Government had entered into six contracts with a contractor to paint and repair certain federal buildings. Each contract was subject to both a performance bond and a payment bond. Although the contractor completed the work on the contracts so that the surety did not have to perform under the performance bond, the surety did pay $13,065.93 on payment bond claims made by laborers and materialmen. Under the terms of the contracts, the Government had retained percentages of the progress

payments due to the contractor, amounting to $12,445.03. Subsequently, the same contractor submitted a bid to the Government for another project, which the Government accepted. However, the contractor failed to enter into a contract for the work, and another contractor performed the job at a price considerably higher than the bid price accepted by the Government, which resulted in damages to the Government in the amount of $6,731.50. In paying over the contract amount that it had retained on the other six contracts to the surety, the Government set off the $6,731.50 it claimed. The surety protested the set-off and asserted its right to an additional $3,568.23. See id. at 332 U.S. 237 - 39, 67 S. Ct. at 1600-01.

With respect to any claims that may have been asserted by the contractor against the Government, the Supreme Court recognized that "[t]he government has the same right `which belongs to every creditor, to apply the unappropriated moneys of his debtor, in his hands, in extinguishment of the debts due to him.'" Id. at 239, 67 S. Ct. at 1602 (quoting Gratiot v. United States, 40 U.S. 336, 370, 10 L. Ed. 759 (1841)). However, the surety argued that it had subrogation rights superior to both the laborers and materialmen to whom the surety had paid and to the Government, the bond obligee. In response to this argument, the Supreme Court observed that:

> [O]ne whose own appropriation and payment of money is necessary to create a fund for general creditors is not a general creditor. He is not compelled to lessen his own chance of recovering what is due him by setting up a fund undiminished by his claim, so that others may share it with him. In

> fact, he is the best of secured creditors; his security is his own justified refusal to pay what he owes until he is paid what is due him.

Id. at 332 U.S. 240, 67 S. Ct. at 1602 (emphasis added). Therefore, the Court held that the Government could set off the amount it claimed. See also United States ex rel. P.J. Keating Co. v. Warren Corp., 805 F.2d 449, 452 (1st Cir. 1986) (recognizing that "Government's set off right is superior to a claim by a Miller Act surety under its payment bond to the same contract earnings"); Marriott Corp. v. Dasto Constr. Co., 26 F.3d 1057, 1070-71 (11th Cir. 1994) (recognizing owner's right to set-off against unpaid contract balance).

National Fire relies on the subsequent Supreme Court decision in Pearlman v. Reliance Ins. Co., 371 U.S. 132, 83 S. Ct. 232, 9 L. Ed. 2d 190 (1962), in which the Court addressed the issue of whether a government contractor's trustee in bankruptcy or the contractor's payment bond surety had the superior right to a fund withheld by the Government out of earnings due to the contractor. The Court recognized the clearly established right of subrogation, which provides that "a surety who pays the debt of another is entitled to all the rights of the person he paid to enforce his right to be reimbursed," and held for the surety. Id., 371 U.S. at 137, 83 S. Ct. at 235. The Supreme Court also noted that the Munsey Trust decision had no effect upon its prior holdings in Prairie State Bank v. United States, 164 U.S. 227, 17 S. Ct. 142, 41 L. Ed. 412 (1896), and Henningsen v. United States Fid. & Guar. Co., 208 U.S. 404, 28 S. Ct. 389, 52 L. Ed. 547 (1908), that "there is a security interest in a withheld fund . . . to which the surety is subrogated." Pearlman, supra, 371 U.S. at 137, 83 S. Ct.

at 235. The Supreme Court construed Munsey Trust as limited to the narrow proposition that "the Government could exercise the well- established common-law right of debtors to offset claims of their own against their creditors." Id. at 140, 83 S. Ct. at 237. Otherwise, the equitable rights of a surety to subrogation were left undisturbed. See id. Therefore, the surety had a superior right, vis-a-vis the principal's trustee in bankruptcy, to funds held by the Government. Pearlman did not involve the priority of rights between a surety and the obligee.

We note that neither Munsey Trust nor Pearlman attempted to differentiate the surety's equitable subrogation rights on the basis of whether a payment or a performance bond obligation had been fulfilled. Under Florida law, which applies here, a performance and payment bond surety's rights to equitable subrogation depend upon the nature of the obligation fulfilled by the surety under the terms of the bonds. In Transamerica Ins. Co. v. Barnett Bank of Marion County, 540 So. 2d 113, 115 (Fla. 1989), the Supreme Court of Florida addressed the issue of "whether a surety's equitable subrogation rights are limited to rights it obtains by standing in the shoes of the defaulting contractor. " In considering this issue, the court observed:

> [T]he surety in cases like this undertakes duties which entitle it to step into three sets of shoes. When, on default of the contractor, it pays all the bills of the job to date and completes the job, it stands in the shoes of the contractor insofar as there are receivables due it; in the shoes of laborers and material men who have been paid by the surety - who may have had liens; and, not least, in the shoes of the

> [obligee], for whom the job was completed.

Id. at 115-16 (quoting National Shawmut Bank v. New Amsterdam Cas. Co., 411 F.2d 843, 844-45 (1st Cir. 1969)). Therefore, "[a] surety who performs or pays on behalf of a [sic] obligee steps into the shoes of the obligee to the extent of performance or payment." Id. at 116 (emphasis added). Thus, only a performance and payment bond surety who pays all of the bills of the job to date and completes the job is entitled to stand in the contractor-principal's shoes and demand payment of unpaid balances from the obligee. The surety's rights, "as subrogee, are not inferior even to the rights of the obligee and may be asserted against the obligee." Id. The Transamerica opinion of the Supreme Court of Florida recognizes that a performing surety may assert a right to contract proceeds superior to the obligee because, by completing the project, the surety conferred a benefit on the obligee and, therefore, stepped into the shoes of the obligee. See id. at 115-16. Where a surety pays the claims of laborers and materialmen, the surety is only entitled to stand in the shoes of those laborers and materialmen who might have had liens, "but for" the surety's payment. Of course, in both cases, the surety's subrogation rights exist only to the extent of the surety's performance. The fact that the surety in this case, National Fire, did not complete performance distinguishes this case from Transamerica. Fn 13

We conclude that National Fire's right to subrogation is controlled by the rationale of the former Fifth Circuit's decision in Trinity Universal Ins. Co. v. United States, 382 F.2d 317 (5th Cir. 1967). Fn 14 In Trinity Universal, the former Fifth Circuit addressed "whether, when a Miller Act surety completes a defaulted contract pursuant to its performance bond, the government may

set off taxes owed by the contractor against the surety's claim to the fund retained by the government to insure performance." Id. at 318. Finding that there was no right to set-off, the former Fifth Circuit recognized that, in Munsey Trust, the rights of the surety were limited to those of subrogee of the contractor because the surety had only performed under a payment bond. Id. at 319. Having made payments pursuant to its payment bond, the surety in Munsey Trust became a creditor of the Government with respect to the funds retained by the Government, and the Government could exercise the well-established common law right to set-off claims against its creditors. Id. at 319-20.

However, the former Fifth Circuit noted that, "[a] different situation occurs when the surety completes the performance of a contract. The surety is not only a subrogee of the contractor, and therefore a creditor, but also a subrogee of the government and entitled to any rights the government has to the retained funds." Id. at 320. The distinction between a surety's rights when performing under a payment bond or a performance bond is important. When a surety completes the project itself or pays the excess completion costs pursuant to the performance bond, the surety confers a benefit upon the obligee, whether the obligee is the Government or a private entity. That benefit relieves the obligee of the burden of completing the construction. In such circumstances, an implicit agreement exists that the surety has a right to all retained funds and any remaining progress sums, and the obligee does not possess a right to set-off. Fn 15 See id. at 320-21; see also Aetna Cas. & Surety Co. v. United States, 435 F.2d 1082, 1083-84 (5th Cir. 1970) (finding that surety's payments made under performance bond were not subject to set-off).

Courts often fail to address the distinction between a surety's right to subrogation when the surety makes payments under a payment bond, as compared to the surety's rights when it performs its performance bond obligations. The payment bond surety, who stands in the shoes of laborers and materialmen, normally has priority with respect to remaining contract balances because those laborers and materialmen would have high priority liens against the property under state law. Under Florida law, construction liens of laborers and materialmen have priority over all subsequently recorded encumbrances on the owner's property. Fla. Stat. § 713.07(3) (1997). Of course, the payment bond surety's subrogation is limited to proper payments made to valid lien claimants. Likewise, the performance bond surety who actually performs stands in the principal's shoes and can demand payment of the remaining contract balances. Further, such a performance bond surety's rights to contract balances are superior to the obligee's and any claims the obligee may have against the principal. Where, as in this case, the surety makes payments under the payment bonds, but does not fulfill its performance bond obligations, this distinction is critical to an equitable prioritization of rights, particularly where it is the obligee who performs in the face of the surety's possible breach of the performance bond.

The rationale of Trinity Universal controls the respective rights of National Fire and Fortune to any retained contract balances in Fortune's possession. To further analyze the surety's subrogation rights, it is necessary to differentiate between what claims are covered by each of the respective bonds. Since National Fire did not complete construction under its performance bonds, it has acquired equitable subrogation rights only with respect to its payment

bonds. The district court erred to the extent that it granted summary judgment for National Fire on its claim of equitable subrogation arising out of the performance bonds. Further, the extent of National Fire's subrogation under the payment bonds to Fortune is limited to the amount of the valid claims National Fire properly paid on a particular project after Fortune's reasonable costs to complete construction on the project are deducted from the remaining contract balances.

Our holding that National Fire is not entitled to equitable subrogation for any performance bond related claims is also based upon our conclusion that the district court erred in its partial summary judgment ruling that National Fire had no obligation under the performance bonds for either project to complete construction itself or to arrange for the completion of construction. Fn 16 Such a ruling would have been correct if the bonds were indemnity-type, but it is undisputed in the record that the performance bonds in this case were not merely indemnity bonds. The touchstone of any right to subrogation under a performance bond is actual and full performance of the bond's obligations. Restatement (Third) of Suretyship & Guaranty § 27 (1995). The language of the two performance bonds plainly contravenes the district court's ruling. The Winston Park performance bond provided that:

> Whenever [Arkin] shall be, and declared by [Fortune] to be in default under the [Winston Park Subcontract], [Fortune] having performed [Fortune's] obligations thereunder, [National Fire] may promptly remedy the default, or shall promptly

> 1) Complete the [Winston Park Subcontract] in accordance with its terms and conditions, or
>
> 2) Obtain a bid or bids for completing the [Winston Park Subcontract] in accordance with its terms and conditions, and upon determination by [National Fire] of the lowest responsible bidder, or if [Fortune] elects, upon determination by [Fortune] and [National Fire] jointly of the lowest responsible bidder, arrange for a contract between such bidder and [Fortune], and make available as Work progresses...sufficient funds to pay the cost of completion less the balance of the contract price; but not exceeding, including other costs and damages for which [National Fire] may be liable hereunder, the amount [of the bond].

Under the terms of this bond, when Arkin was declared in default, National Fire had three options: (1) it could remedy the default; (2) it could complete construction itself; or (3) it could arrange for the completion of construction by selecting, either by itself or jointly with Fortune, a completion contractor and by making funds available to the completion contractor for completion costs in excess of the contract price. National Fire could not, as the district court held, merely ignore Fortune's demands that National Fire perform, force Fortune to complete construction, and then pay Fortune for reasonable costs in excess of the contract price. The express terms of the Winston Park performance bond placed the burden of performance on National Fire. Because National Fire did not perform, it is not entitled

to subrogation with respect to the Winston Park performance bond.

The district court also erred in applying the same analysis to National Fire's West Brickell performance bond obligation as to the Winston Park performance bond obligation. Unlike the Winston Park performance bond, the West Brickell performance bond's terms potentially contemplated completion of construction by Fortune. The West Brickell performance bond stated: Whenever [Arkin] shall be, and be declared by [Fortune] to be in default under the subcontract, [Fortune] having performed [Fortune's] obligations thereunder:

> (1) [National Fire] may promptly remedy the default subject to the provisions of paragraph 3 herein; or
>
> (2) [Fortune] after reasonable notice to [National Fire] may, or [National Fire] upon demand of [Fortune] may arrange for the performance of [Arkin's] obligation under the subcontract subject to the provisions of paragraph 3 herein;
>
> (3) The balance of the subcontract price ... shall be credited against the reasonable cost of completing performance of the subcontract. If completed by [Fortune], and the reasonable cost exceeds the balance of the subcontract price, [National Fire] shall pay to [Fortune] such excess, but in no event shall the aggregate liability of [National Fire] exceed the amount of this bond.
>
> (Emphasis added).

Under this provision, National Fire also had three alternatives: (1) it could remedy the default; (2) if Fortune provided National Fire reasonable notice that Fortune wished to arrange for completion, it could allow Fortune to arrange for the completion of construction; or (3) if Fortune demanded that National Fire arrange for completion of construction, it could arrange for completion of construction itself. According to the evidence in the record (and construing the record in the light most favorable to Fortune since it appears to be a genuine factual dispute), Fortune did not wish to complete construction of the West Brickell project itself after Arkin defaulted. Instead, Fortune demanded that National Fire arrange for completion of construction of the West Brickell project, and National Fire refused to do so. Paragraph three of the West Brickell performance bond does contemplate the possibility that Fortune could have completed the subcontract itself. However, this contingency would only occur if, under the second alternative, Fortune sought to complete construction itself or, under the third alternative, National Fire arranged for Fortune to complete construction. In either of these cases, Fortune (not National Fire) could choose whether Fortune would voluntarily complete construction. Because it appears National Fire did not perform, it is not entitled to subrogation with respect to the West Brickell performance bond.

We also find that disputed issues of material fact exist in the record about whether National Fire's failure to perform amounted to a breach of its performance bond obligations, as described above. National Fire claims it appropriately tendered a completion contractor and that Fortune refused this tender. (Aff. of Raymond Lemming, R.27 at 4-5.) Fortune claims a completion contractor was never tendered despite its demands. (Aff. of Michael Getz, R.44 at 2.) This obvious factual conflict

was presented to the district court in the parties' arguments on National Fire's motions for partial summary judgment. The only way the district court avoided confronting this conflict was by erroneously ruling that, as a matter of law and without reference to the language of the performance bonds, National Fire had no obligation to tender a completion contractor or to complete performance itself. Summary judgment on Fortune's breach of contract claim against National Fire was improper and we remand for further proceedings on this issue. Fn 17

A. Fortune's Setoff Claims

Having concluded that National Fire is only entitled to equitable subrogation with respect to valid payments made under its payment bonds, and that Fortune is entitled to a setoff for all items encompassed within the scope of the performance bonds, we now must consider the specific claims for which Fortune seeks setoff.

1. Liquidated Delay Damages

Fortune contends that National Fire is responsible for liquidated delay damages that had accrued prior to Arkin's default due to Arkin's failure to timely perform on both projects. Although Fortune obtained judgment as a matter of law against Arkin for these damages, Fortune seeks to set these damages off against the retained contract balances. Fortune also argues that National Fire is contractually liable for these damages because the bonds incorporated by reference the underlying subcontracts which expressly provided for delay damages. However, National Fire denies any responsibility for delay damages, arguing that such damages are unrelated to the completion of the bonded

construction projects and that the performance bonds do not expressly recognize liability for delay damages.

We look to Florida law to see what a surety's obligations are in the circumstances of this case. As a general proposition, the true performance bond requires a surety to guarantee the performance through completion of the underlying contract. See Federal Ins. Co. v. Southwest Fla. Retirement Ctr., Inc., 707 So. 2d 1119, 1121 (Fla. 1998). However, in American Home Assurance Co. v. Larkin General Hospital, Ltd., 593 So. 2d 195 (Fla. 1992), the Supreme Court of Florida held that "a surety cannot be held liable for delay damages due to the contractor's default unless the bond specifically provides coverage for delay damages." Id. 593 So. 2d at 196 (footnote omitted). In Larkin General Hospital, the contractor had not substantially completed the project by the target date, but the owner did not declare the contractor in default. Nearly eighteen months later, after a dispute arose between the owner and contractor, the owner declared the contractor in default and notified the surety. The surety elected not to complete performance and the owner used another contractor to complete the job. In the owner's action against the surety for breach of the performance bond, the trial court included in its damage award the owner's consequential delay damages for the contractor's tardy performance. Importantly for purposes of our analysis, there was no liquidated or other type of damages provision in the underlying contract. The Larkin General Hospital court noted:

> [t]he purpose of a performance bond is to guarantee the completion of the contract upon default by the contractor. Ordinarily a performance bond only ensures the completion of the contract. The surety

> agrees to complete the construction or to pay the obligee the reasonable costs of completion if the contractor defaults.

Id. at 198 (citations omitted). Although a surety's liability is coextensive with that of the principal, "the surety's liability for damages is limited by the terms of the bond." Id. Therefore, the Supreme Court of Florida found that "[t]he language in the performance bond, construed together with the purpose of the bond, clearly explains that the performance bond merely guaranteed the completion of the construction contract and nothing more." Id. (emphasis added); see also Mycon Constr. Corp. v. Board of Regents, 755 So. 2d 154, 155 (4th DCA 2000) ("Because the performance bond contains no provision for damages for delay, the surety cannot be held liable for such damages."). However, unlike the performance bond in Larkin General Hospital, the bonds at issue in this case expressly incorporated the subcontracts, which, in turn, do expressly provide for liquidated delay damages.

Larkin General Hospital could possibly be interpreted to mean that a performance bond surety cannot be held liable for, or denied subrogation for, delay damages, whether liquidated or unliquidated, unless the responsibility for delay damages is specified on the face of the performance bond. However, we do not read the decision that broadly. Fn 18 The "purpose of the bond" must be considered, which requires reference to the contract secured by the bond. Where a provision for liquidated delay damages is clearly delineated in the underlying contract and incorporated by reference into the bond, the surety is on notice of the time element of performance and the contractual consequences of failure to timely perform in accordance with the contract. Once the liquidated damages accrue, the

contractor- principal owes a debt to the obligee which is, in effect, a reduction of (or contractual off-set to) the contract price. In such event, the obligee becomes the creditor of the principal and the performance bond surety should not have superior rights to the obligee in the remaining contract balances where liquidated damages have been suffered. This is especially true where, as here, the surety does not remedy the principal's delay by performing the surety's obligations under the performance bond.

While it is true that the terms of the bonds in this case do not expressly require the surety to assume responsibility for delay, "[i]t is the general rule of contract law that where a writing expressly refers to and sufficiently describes another document, the other document is to be interpreted as part of the writing." Lord & Son Constr., Inc. v. Roberts Electrical Contractors, Inc., 624 So. 2d 376, 377 n.2 (Fla. 1st DCA 1993). Even after Larkin General Hospital, Florida courts have continued to utilize the well-established doctrine of incorporation by reference to impose liability on a performance bond surety. See DCC Constructors, Inc. v. Randall Mech. Inc., 791 So. 2d 575, 576-77 (Fla. 5th DCA 2001); Southwest Fla. Retirement Ctr. v. Fed Ins. Co., 682 So. 2d 1132-33 (Fla. 2d DCA 1996), aff'd, 707 So. 2d 1119 (Fla. 1998). The "purpose" of the performance bonds was to insure performance in accordance with the terms of the respective subcontracts, and those terms plainly include adverse direct consequences for delay. Therefore, under the particular facts of this case, the unequivocal delay damages provisions of the subcontracts are properly considered part of the bonds issued by National Fire because of the incorporation by reference. Moreover, the liquidated delay damages are properly considered part of the performance of the subcontracts, and it is

undisputed that Fortune completed the projects, with no performance-related costs being incurred or paid by National Fire. Accordingly, Fortune's claim for set-off of the delay damages is entitled to priority over National Fire with respect to any of National Fire's claims related to the performance bonds.

However, Fortune's claim for delay damage set-off is not entitled to priority over National Fire's valid payment bond claims. A performing payment bond surety stands in the shoes of the laborers and materialmen who might have had liens on the property. That right is generally superior to the rights of either the principal or the obligee. To the extent of the payment bond claims actually and properly paid, National Fire's right to any unpaid contract balances is superior to Fortune's liquidated delay damages claim. Fn 19 We express no opinion about whether National Fire may be responsible for delay damages related to Fortune's breach of contract claims on the performance bonds.

2. Davis-Bacon Wages

The district court granted National Fire partial summary judgment on Fortune's counterclaim for set-off of the amount of back wages Fortune paid due to violations of the Davis-Bacon Act by one of Arkin's subcontractors on the West Brickell Project. The Davis-Bacon Act requires laborers on federally funded projects to be paid not less than the "prevailing" wages in the locale. See 40 U.S.C. § 276a(a); Walsh v. Schlecht, 429 U.S. 401, 411, 97 S. Ct. 679, 686, 50 L. Ed. 2d 641 (1977). The Act requires that "every contract based upon these specifications shall contain a stipulation that the contractor or his subcontractor shall pay all mechanics and laborers" the federally mandated wages. 40 U.S.C. § 276a(a) (emphasis added). Federal regulations applicable to

contracts and subcontracts under the Davis-Bacon Act provide, "The prime contractor shall be responsible for the compliance by any subcontractor or lower tier subcontractor...." 29 C.F.R. § 5.5(a)(6) (1999).

We conclude that the Davis-Bacon wages paid by Fortune are part of Fortune's reasonable cost of completion of construction. Fn 20 The Davis-Bacon wage claims paid by Fortune represent wages of laborers on the West Brickell project that should have properly been paid as part of the costs of construction. Because of Arkin's failure to properly supervise Allied's compliance with the Davis-Bacon Act, as Arkin was required to do under the West Brickell Subcontract, federal funds payable to Fortune, as general contractor, for the West Brickell project sufficient to pay Allied's employees could have been withheld. 40 U.S.C. § 276a-2(a). If the remaining federal funds were insufficient to repay the employees, the Davis-Bacon Act gave Allied's employees the right to file a lien on the West Brickell property for the difference. 40 U.S.C. § 276a-2(b); Fla. Stat. § 713.03. We reverse the district court's grant of partial summary judgment to National Fire on this issue and hold that Fortune has a right to set off its $71,126.00 Davis-Bacon Act claim against the remaining contract balances as part of Fortune's reasonable costs of completion. Fn 21

3. Electrical Overages

Fortune also claims the Fortune-Arkin letter agreement gives Fortune a right to payment from National Fire for the electrical overages Fortune paid on the West Brickell project. However, the West Brickell performance bond cannot be construed to cover an agreement that was not identified in the West Brickell Subcontract. Fn 22 The West Brickell performance bond

specifically incorporated the West Brickell Subcontract by reference. The list of "Contract Documents" identified in the West Brickell Subcontract, which sets forth the documents that are part of the bonded subcontract, does not include the letter agreement. The subcontract made no other reference to the letter agreement, even though the parties made several other handwritten alterations to the subcontract. Merger and integration provisions in both the "Contract Documents" section and in Article 17 of the subcontract provide that the referenced documents are the entire and complete agreement of the parties. Since the bond was issued on the subcontract without reference to the letter agreement, the letter agreement is not within the scope of contract work that National Fire agreed to insure when it issued the bond. Further, the district court properly rejected Fortune's offer of parol evidence that the letter agreement was part of the subcontract because Fortune produced no evidence that National Fire knew of the letter agreement at the time it issued the bond. Therefore, Fortune has no right to payment for electrical overages from National Fire and the district court properly granted summary judgment in favor of National Fire on this issue.

C. Remaining Issues

1. National Fire's Breach of Contract Claim

Fortune argues that National Fire's breach of contract claim should not have been submitted to the jury because Fortune was not a signatory to the performance bonds on which the claim was based. National Fire asserts that the terms of the bond obligated Fortune to pay National Fire the balance of the proceeds of the Fortune-Arkin subcontract after Fortune completed

construction. The terms of the bonds plainly contradict National Fire's argument. Normally, bond agreements create duties that run from the surety to the obligee. The obligee is a beneficiary of the agreement between surety and principal. While there may possibly be some circumstances under which a bond's terms might impose duties on the obligee, Fortune was merely a beneficiary of the performance bonds here. Fn 23 As discussed above, bonds are to be interpreted according to ordinary principles of contract construction. American Home Assurance Co. v. Larkin Gen. Hosp., Ltd., 593 So. 2d at 195, 197 (Fla. 1992); Restatement (Third) of Suretyship & Guaranty §§ 17(2), 32(1) (1995).

In the event that Arkin defaulted, under the terms of both performance bonds National Fire could complete construction itself or agree with Fortune to jointly select another contractor to finish construction, which could possibly be Fortune if the parties so agreed. If the latter occurred, the performance bonds obligated National Fire to make available funds for the completion of construction to the extent the costs exceeded the balance of the contract price. This provision does not require Fortune to tender to National Fire the remaining contract price if Fortune completed construction at a cost less than the contract price. Our interpretation of the bonds' terms is consistent with the surety's traditional duty to complete construction in the event of the principal's default. The purpose of a performance bond is to assure the obligee that construction will be completed and that it will not be liable for construction costs in excess of the contract price in the event the contractor defaults. If National Fire had completed construction, it would have been entitled to payment of the contract price, or under equitable subrogation, entitled to the remaining contract balances held by Fortune. However, National Fire did not complete

construction under the bond's terms. Instead, Fortune completed construction and, luckily for National Fire, at a cost less than the contract price. Under no reasonable construction of the performance bonds' terms can a contractual duty be found for Fortune to pay National Fire the remaining balance after Fortune completed construction. Therefore, the district court erred in allowing National Fire's breach of contract claim to be submitted to the jury. Further, even if (as National Fire claims) Fortune did prevent National Fire from completing construction by refusing to accept National Fire's tender of a completion contractor, National Fire could only assert this fact as an affirmative defense that its liability under the performance bonds was discharged, not as a breach of contract claim against Fortune. See Ins. Co. N. Amer. v. Metro. Dade County, 705 So. 2d 22, 34-35 (Fla. 3d DCA 1997)(obligee's failure to timely notify surety of latent defects discharged surety). See also St. Paul Fire & Marine Ins. Co. v. City of Green River, 93 F. Supp. 2d 1170 (D. Wyo. 2000), aff'd, 2001 WL 369831 (10th Cir. 2001).

2. Prejudgment Interest

Finally, we consider the district court's award of prejudgment interest on the jury's damages verdict in favor of National Fire, retroactive to January 30, 1998. Fortune notes that National Fire did not pay one payment bond claimant on the West Brickell project until March 19, 2001, and last paid a like claimant on the Winston Park project on May 15, 2001. Fortune argues that any equitable subrogation rights did not accrue until those dates, when performance under the bonds was complete. Therefore, Fortune contends that prejudgment interest should have been calculated from those dates on the respective projects, and not over three years earlier.

We agree. Prejudgment interest in an action for breach of contract is allowable from the date the debt is due. See, e.g., Paoli v. Natherson, 732 So. 2d 486, 488 (Fla. 2d DCA 1999). Where the judgment liquidates the plaintiff's damages, the plaintiff is entitled, as a matter of law, to prejudgment interest from the date of that loss. Argonaut Ins. Co. v. May Plumbing Co., 474 So. 2d 212, 215 (Fla. 1985). However, in this case, National Fire's right to equitable subrogation under its payment bonds with respect to the remaining contract balances did not arise until all of its payment bond obligations had been performed. Restatement (Third) of Suretyship & Guaranty § 27 (1995). Further, any entitlement to equitable subrogation on the remaining contract balances could not be determined until after Fortune had completed the construction. If, as is usually the case, the cost of completion by Fortune had equaled or exceeded the contract price, there would have been no remaining balances and National Fire would not have been entitled to any equitable subrogation with respect to them. The district court erred when it awarded prejudgment interest on National Fire's equitable subrogation claim prior to the completion of its payment bond obligations.

IV. CONCLUSION

For the above reasons, the judgment of the district court is AFFIRMED IN PART and REVERSED IN PART and this case is REMANDED for further proceedings consistent with this opinion.

FOOTNOTES

Fn* Honorable Roger Vinson, United States District Judge for the Northern District of Florida, sitting by designation.

Fn 1 AIA Document A311.

Fn 2 The typed letter, dated January 15, 1996, signed by both Fortune and Arkin, stated in pertinent part:

> RE:Construction Contract dated January 15, 1996 for West Brickell Apartments
>
> Dear Mr. Arkin:
>
> The Schedule of Values attached to the . . . contract . . . states that the electrical, elevator and cabinet trades have been excluded from said contract. The agreement between Fortune and Arkin is that even though these items have been excluded from said Contract, and despite the fact that the contracts with these trades are to be signed by Fortune (not Arkin), Arkin takes full responsibility for cost overages should the contract amounts for each of these trades exceed the following figures: (a) electrical - $669,000, (b) elevator - $185,000 and (c) cabinets - $110,916.
>
> This responsibility on the part of Arkin includes, but is not limited to, either Arkin finding a replacement subcontractor to contract for the specific trade at the above referenced amounts, or Arkin issuing a credit change order to Fortune for any amounts over and above the above referenced figures. . . .
>
> (R.85, Ex. C.)

Fn 3 The affidavits of Michael Spetko, the Project Manager for the West Brickell project, and Ernesto Gordo, an employee of Fortune who participated in negotiating the West Brickell Subcontract with Arkin are in the record. (R.89.) In these affidavits, Spetko and Gordo assert that they were involved in negotiating the subcontract and that the letter agreement was intended by both Arkin and Fortune to be an integral part of the subcontract on the West Brickell project. Gordo added that the letter agreement was made an addendum to the subcontract. There is nothing in writing evidencing incorporation of the letter agreement.

Fn 4 Fortune retained possession of certain proceeds from the two subcontracts pursuant to retainage and progress-payment provisions of the subcontracts. However, the exact amount of contract balances remaining is a matter of dispute between the parties.

Fn 5 Each motion addressed a discrete legal issue, and five of the motions were simultaneously filed. We discourage this practice of unnecessarily filing multiple motions for partial summary judgment. While the legal issues in this case are complex, combining the various legal issues into a single motion would have helped the trial court achieve a broader understanding of the entire case. National Fire's attempt to break this case into little pieces seems to have contributed to the confusion below. See also S.D. Fla. Loc. R. 7.1(C)(2).

Fn6 As noted earlier, the documents were different for each project. From examining the language quoted by the district court, we determine that the court cited the Winston Park performance bond. The district court made reference to neither the language of the West Brickell performance bond nor either of the two payment bonds.

Fn 7 Again, in making this determination, the district court did not cite any of the operative language from any of the bonds in support of its ruling. National Fire's performance obligations materially differed under the two performance bonds.

Fn 8 Because National Fire did not pursue its assignment claim, the district court granted Fortune judgment as a matter of law as to that claim.

Fn 9 The district court instructed the jury that, in making this determination, the jury was not to include unreasonable costs Fortune could have avoided, costs related to correcting design defects, the liquidated delay damages, costs for electrical overages, and the Davis-Bacon wage claims. (R.133 at 9, 10, 12.)

Fn 10 Specifically, the district court instructed the jury:

> The Court has found, as a matter of law, that National Fire has a right to recoup payments it made under the payment bonds from the unpaid balance of the subcontract. This right is superior to Fortune's right to apply the unpaid balance of the subcontract to claims that it might have against Arkin. The Court having so determined, this issue is not for your consideration.
>
> The Court has also previously determined that, at this juncture, the reasonable costs of completing construction are to be credited against the contract balance....[T]o the extent the contract balance exceeds the reasonable costs of completing construction, the excess is to

be paid to National Fire up to the amount of National Fire's payment bond expenditures.

***

In determining the reasonable cost to complete the projects, the Court has previously determined that certain damages and consequential post default costs that may have been incurred by Fortune must not be considered part of the reasonable cost to complete the projects and may not be assessed against National Fire. These include: (1) delay damages, including liquidated damages specified in the Arkin subcontracts; (2) damages relating to Fortune's electrical overage claim; (3) damages relating to Fortune's Davis-Bacon Act claim. While these items may constitute proper claims against Arkin, they are not to be considered part of the reasonable cost to complete the projects and may not be applied against National Fire.

***

In determining whether National Fire breached the performance bond, you must accept that the Court has previously determined that National Fire had no obligation to complete the project itself or to tender a completion contractor. Rather, National Fire's only performance bond obligation is to pay any excess, should it exist, of the reasonable cost to complete

by Fortune over the contract balance at the time of default by Arkin.

(R.133 at 7, 12, 20).

Fn 11 Part of the jury's consideration in awarding National Fire damages was the determination of the reasonable costs of completion. However, the verdict form did not require the jury to make a specific finding as to the reasonable completion costs or as to the contract balances remaining before deductions. Instead, the jury merely calculated the remaining contract balances after reasonable completion costs and other costs were deducted. We have labored to try to infer the completion costs and remaining balances in light of the jury's verdict, but we have been unable to do so.

Fn 12 Fortune contends that equitable subrogation is not appropriate because National Fire did not complete, pursuant to its performance bonds, either the West Brickell or the Winston Park projects, and issues of fact exist concerning whether National Fire paid all of its payment bond obligations. See Affidavit of Michael J. Getz (listing unpaid subcontractors, laborers, and materialmen) (R.44.) From the record, it appears that one sub-subcontractor, Aurora Plumbing Corp., was pursuing a payment claim in state court at the time of trial. (R.149 at 55-59.) National Fire, however, represents that it fully satisfied its payment obligations by paying over $1.4 million in payment bond claims, which amounted to every claim timely submitted. For purposes of this appeal, we have assumed that the district court has resolved all factual issues with respect to the payment bond claims.

Fn 13 "Subrogation rights place a party . . . in the legal position of one who has been paid money because of the

acts of a third party. Thus, the subrogee `stands in the shoes' of the subrogor and is entitled to all of the rights of its subrogor, but also suffers all of the liabilities to which the subrogor would be subject.'" Cleary Bros. Constr. Co. v. Upper Keys Marine Constr., Inc., 526 So. 2d 116, 117 (Fla. 3d DCA 1988) (quoting Allstate Ins. Co. v. Metropolitan Dade County, 436 So. 2d 976, 978 (Fla. 3d DCA 1983)).

Fn 14 The Eleventh Circuit has adopted as precedent decisions of the former Fifth Circuit rendered prior to October 1, 1981. See Bonner v. Prichard, 661 F.2d 1206 (11th Cir.1981).

Fn 15 In Dependable Ins. Co. v. United States, 846 F.2d 65 (Fed. Cir. 1988), the Federal Circuit also recognized that a surety's subrogation rights, with respect to set-offs asserted by the Government, vary depending upon whether the surety performed under a performance bond or a payment bond. In that case, the surety acknowledged that, under Munsey Trust, "the government's right to retained contract proceeds are generally superior to those of a payment bond surety." Id. at 67. The Federal Circuit further explained why performing performance bond sureties have superior rights to the obligee, while payment bond sureties do not:

> [W]hen a surety finances completion of a project, it confers a benefit upon the government by relieving it of the task of completing performance itself. It therefore becomes subrogated not only to the rights of the prime contractor but to those of the government. Accordingly, a completing performance bond surety has the right to accumulated contract proceeds free from setoff by the government.

Id. at 67.

Fn 16 National Fire could not, as the district court ruled, simply "do nothing" and pay for any excess construction costs. As noted in one treatise:

> The seductive enticement of the `do nothing' option to the surety is avoiding the immediate cost of completion, but this course of action remains advantageous only if the surety is correct in its analysis that it has no liability to the obligee....Some bond forms remove the surety's `do nothing' option. These instruments require the surety to act. If the surety believes it has a defense, it may reserve its rights and litigate – but it must perform.

Phil Bruner & Patrick O'Connor, 4 Bruner & O'Connor on Construction Law § 12:82 n.5 (2002), WL BOCL § 12:82.

Fn 17 Determination of the factual dispute about whether National Fire actually breached the performance bonds is unnecessary to our ruling on National Fire's claim of equitable subrogation. It is undisputed that National Fire did not, in fact, complete construction, and for that reason National Fire cannot claim subrogation under the performance bonds.

Fn 18 The Supreme Court of Florida has since declined to extend Larkin General Hospital beyond delay damages. Federal Ins. Co. v. Southwest Fla. Retirement Ctr., 707 So. 2d 1119, 1121 (Fla. 1998).

Fn 19 It is not clear from the record, but it appears that National Fire's payment bond equitable subrogation claims may exhaust the contract balances retained by Fortune.

Fn 20 One could evaluate Fortune's Davis-Bacon Act claim, as Fortune suggests, as part of National Fire's performance bond obligation because the West Brickell performance bond specifically incorporated by reference the West Brickell Subcontract which imposed on Arkin the responsibility for Arkin's subcontractors' acts and omissions. However, we think the Davis-Bacon Act wages are properly considered costs of construction because they represent wages that should have properly been paid, and were paid, through enforcement by the Department of Labor, to the laborers on the West Brickell project. Such wages were a part of the cost of completion.

These wages could also be considered as being within National Fire's payment bond obligation, but because of unique language in the West Brickell payment bond, the Davis-Bacon wage claims escape coverage under the bond. National Fire was only obligated under the West Brickell payment bond to make payments to valid "claimants", defined as those persons having a "direct contract" with Arkin. The Davis-Bacon wage claimants were employees of Allied who did not technically have a "direct contract" with Arkin.

Fn 21 The parties also have raised an issue concerning whether public policy favors holding either the principal contractor or a subcontractor's surety responsible for ensuring payment of Davis-Bacon wages. As discussed earlier, Fortune is required by law, as well as by public policy, to ensure compliance by its subcontractors with the Davis- Bacon Act. See 40 U.S.C. §276a; 29 C.F.R.

§5.5(a)(6). Fortune satisfied this responsibility in the West Brickell Subcontract, which was incorporated by National Fire's performance bond, by requiring Arkin to be responsible for the acts and omissions of its subcontractors. We first note that Fortune actually paid the Department of Labor's Davis-Bacon Act claim for restitution. Fortune only seeks reimbursement from Arkin and National Fire for their failure to pay the claim when requested to do so. Moreover, in the West Brickell performance bond, National Fire necessarily accepted the risk that its principal, Arkin, would not fulfill these obligations imposed upon it by the Act and its subcontracts. As a result, we conclude that the policy behind the Davis-Bacon Act will not be frustrated by allowing Fortune to recover this amount as a part of its reasonable costs of completion.

Fn 22 According to Fortune, the letter agreement dated January 15, 1996, is included in the bonded West Brickell Subcontract as evidenced by the fact that National Fire admitted its inclusion in its Answer to Fortune's counterclaim. At oral argument, counsel for Fortune indicated that this admission by National Fire had not been brought to the trial judge's attention prior to the granting of summary judgment against Fortune. Counsel for National Fire indicated that the admission was inadvertent. It appears that National Fire did erroneously admit that this agreement was part of the bonded subcontract, but we do not believe that this inadvertent admission should control liability for these overage costs when it was not considered by the district court.

Fn 23 Even if the agreement imposed duties on Fortune, we find it difficult to understand how a principal and surety could bind an obligee to perform those duties without expressly obtaining the obligee's consent.

Case No. 97-2439 CIV-KING

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

NATIONAL FIRE INSURANCE COMPANY
OF HARTFORD, a Connecticut corporation.
Plaintiff,

V.

FORTUNE CONSTRUCTION COMPANY.
A Florida corporation,

V.

ARKIN CONSTRUCTION COMPANY, INC.
Third Party Defendant.

JUDGMENT

This action came on for trial before the Court and a jury, Honorable James Lawrence King. Senior Judge, presiding, and the issues having been duly tried and a decision having been duty rendered, it is

ORDERED AND ADJUDGED:

That the plaintiff, National Fire Insurance Company of Hartford, recover from the Defendant, Fortune Construction Company, the sum of $592,670.28, plus prejudgment interest in the sum of $206.680.24, for which let execution issue. The sum of $799,350.52 shall bear post-judgment interest at the rate of 3.70%. The Court reserves jurisdiction on issues related to the recovery of fees and costs.

That the defendant, Fortune Construction Company, shall take nothing on its counterclaim against plaintiff. National Fire Insurance Company, and this action shall be dismissed on the merits.

DATED this 23rd day of July, 2001.

JAMES LAWRENCE KING
UNITED STATES DISTRICT
JUDGE

Case No. 97-2439 CIV-KING

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

NATIONAL FIRE INSURANCE COMPANY
OF HARTFORD, a Connecticut corporation.
Plaintiff,

V.

FORTUNE CONSTRUCTION COMPANY.
A Florida corporation,

V.

ARKIN CONSTRUCTION COMPANY, INC.
Third Party Defendant.

ORDER GRANTING PLAINTIFF'S MOTION FOR PARTIAL SUMMARY

THIS CAUSE comes before the Court on Plaintiff's several Motions for Partial Summary Judgment, filed June 8, 1998. Defendant Fortune ("Fortune") filed its reply on June 24, 1998. The Court heard oral argument on July 10, 1998, at which the parties argued their respective positions on the issue of equitable subrogation.

Background

Arkin Construction Company, Inc. ("Arkin") subcontracted with Fortune to build two apartment complexes. In December 1995, Plaintiff ("National Fire") entered into a general indemnity agreement with Arkin. Pl.'s Ex. A. Fortune was not and is not a party to that

agreement. Pursuant to the indemnity agreement, National Fire as surety and Arkin as principal issued Transamerica Ins. Co. v, Barnett Bank of Marion County 540 So. 2d 113, 116-117 (Na. 1989)(citing Pearlman v. Reliance Ins. Co., 371 U.S. 32 (1962)). The Court finds that Plaintiff has a right to recoup payments it made under the payment and performance bonds from the unpaid balance of the subcontract, this right being superior to Defendant's right to apply that balance tq claims it may have against the defaulting subcontractor.

Accordingly, after a careful review of the record and the Court being otherwise fully advised, it is

ORDERED and ADJUDGED that PlaintifFs Motion for Partial Summary Judgment be, and the same is hereby, GRANTED.

DONE and ORDERED in chambers at the James Lawrence King Federal Justice Building and United States District Courthouse, this 10th day of July, 1998.

JAMAES LAWRENCE KING
U.S. DISTRICT JUDGE
SOUTHERN DISTRICT OF
FLORIDA

No. 01-15124-FF

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH DISTRICT

NATIONAL FIRE INSURANCE
COMPANY OF HARTFORD,
Plaintiff-Counter-
Defendant-Appellee,

versus

FORTUNE CONSTRUCTION COMPANY,
Defendant-Counter-
Claimant-Third-Party-
Plaintiff-Appellant,

ARKIN CONSTRUCTION COMPANY, INC.,
Third-Party-Defendant

On Appeal from the United States District Court
for the Southern District of Florida

BEFORE: TJOFLAT and KRAVITCH, Circuit Judges,
and VINSON*, District Judge.

PER CURIAM:

The petition(s) for rehearing filed by Appellee is DENIED.

ENDERED FOR. THE COURT:

UNITED STATES CIRCUIT JUDGE

*Honorable Roger Vinson, United States District Judge for the Northern District of Florida, sitting by

designation.

United States Court of Appeals
Eleventh Circuit
56 Forsyth Street, NW.
Atlanta, Georgia 30303

April 01, 2003

MEMORANDUM TO COUNSEL OR PARTIES

RE: 01-15124-FF National Fire Insurance v. Fortune Construction DC DKT NO.: 97-02439 CV - JLK

The enclosed order has been entered on petition(s) for rehearing.

See Rule 41, Federal Rules of Appellate Procedure, and Eleventh Circuit Rule 41-1 for information regarding issuance and stay of mandate.

Sincerely,

THOMAS K. KAHN, Clerk

Reply To: April Richards (404) 335-6179

Encl.

Case No. 97-2439 CIV-KING

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

NATIONAL FIRE INSURANCE COMPANY
OF HARTFORD, a Connecticut corporation.
Plaintiff,

V.

FORTUNE CONSTRUCTION COMPANY.
A Florida corporation,

V.

ARKIN CONSTRUCTION COMPANY, INC.
Third Party Defendant.

PRETRIAL CONFERENCE ORDER

THIS CAUSE came before the Court for Pretrial Conference on July 15, 1998. The Court heard oral arguments on various issues of law which are ripe for ruling.

Background

Arkin Construction Company, Inc. ("Arkin") subcontracted with Fortune Construction Company ("Fortune") to build two apartment complexes, In December, 1995, National Fire Insurance Company of Hartford ("National Fire") entered into a general indemnity agreement with Arkin. Pl's Ex. A. Fortune was not and is not a patty to that agreement. Pursuant to the indemnity agreement, National Fire, as surety, and Arkin, as principal, issued Performance and Payment Bonds for the construction project. Pl's Ex. B and C. On

May 29, 1997, Arkin abandoned the construction projects and Fortune declared Arkin in default of the construction subcontracts on June 12, 1997.

The construction projects were completed by Fortune as general contractor. National Fire paid sums to payment bond claimants on both projects.

In its previous Order, this Court held that National Fire

> [h]as a right to recoup payments it made under the Payment and Performance Bonds from the unpaid balance of the subcontract, this right being superior to Defendant's right to apply that balance to claims it may have against defaulting subcontractor.

Order of July 10, 1998 at 3. Thus, at this junctur, the reasonable costs of completing construction are to be credited against the contract balance. To the extent those costs exceed the contract balance, National Fire is obligated pursuant to the Performance Bond to pay the difference to Fortune. Conversely, to the extent the contract balance exceeds the reasonable costs of completing construction, the excess is to be paid to National Fire up to the amount of National Fire's payment bond expenditures.

Discussion

Three legal issues remain for determination by the Court. The most substantial is whether certain consequential, post default costs allegedly incurred by Fortune are recoverable against the National Fire bonds. Those alleged costs consist of interest expense on construction loans, real estate taxes, insurance,

administrative and leasing salaries, marketing/leasing expenses, legal fees and lost rentals. These costs are alleged to have been incurred because the projects were not completed on the original schedule. However, there is no indication that, after Arkin's default, Fortune did not complete on a timely basis.

Just as National Fire was not responsible for liquidated damages incurred by Arkin prior to default, National Fire is also not responsible for consequential time-related damages allegedly incurred after default unless those damages are the direct consequence of National Fire's own act. Bill Curphy Co. v. Elliot, 207 F. 2d 103, (5th Cir. 1953).

Fortune argues that National Fire breached its Performance Bond obligations by failing to take over and complete construction itself or to formally tender a completion contractor. However, National Fire had no obligation to complete or tender, but rather its obligation was to pay the excess of the costs to complete qver the contract balance, if any. United States v. Seaboard Surety Co., 817 F. 2d 956 (2d Cir. 1987). Therefore even if, as alleged., National Fire did not complete with its own forces or formally tender a completion contractor, that does not constitute a breach of the Performance Bond contract from which consequential damages may flow. See American Home Assurance Co. v, Larkin, 593 So. 2d 195 (Fla 1992); 5. Myers, Performance Bonds and Guarantees; Current Issues, 501 PLI/Comm 429 (1989).

In addition, Fortune's alleged consequential damages are calculated commencing with the day after the default of Arkin. Yet, no matter what National Fire may have done or not done, it would not achieve completion of construction instantaneously. If National Fire were

otherwise liable for consequential damages, it would have to be permitted a reasonable time for completion of construction prior to commencement of such damages. Thus, even if there were a breach of the Performance Bond obligation by National Fire, which has not occurred here, Fortune would have the burden of proving any consequential damages which proximately flowed from that breach, rather than from the breach of Arkin. See, Trainor Co. v. Aetna Casualty Co., 290 U.S. 47 (1933).

Finally, Fortune points out that National Fire loaned money to Arkin to fund overhead expenses for a period of time while National Fire conducted its investigation. Fortune argues that commencement of this funding placed an obligation on National Fire to continue it through completion of the project.

There is no dispute that National Fire has no obligation to fund Arkin. Transamerica Premier Ins. Co. v. K S Constr., 850 F.Supp. 930 (D. Cob. 1994). The Court finds as a matter of law that providing such funding for a period of time did not give rise to any obligation to continue to finance. Transamerica 850 F. Supp. at 934. See also, John G. Lambros Co. Inc. v. Aetna Casualty & Surety Co., 468 F. Supp. 624 (S.D.N.Y, 1979). Therefore, the cessation of financing does not constitute a breach of the Performance Bond contract.

Accordingly, after a careful review of the record and the Court being otherwise fully advised, it is

ORDERED and ADJUDGED that:

1. National Fire had no obligation to formally tender a completion contract or a finished project, but rather could meet its obligations by paying the

reasonable costs of completion should they exceed the contract balances.

2. National Fire had no obligation to finance Arkin or to continue financing Arkin once it temporarily agreed to do so.

3. National Fire is not liable for consequential damages after default which were not the result of a breach of the Performance Bond obligation.

DONE and ORDERED in Chambers at the James Lawrence King Federal Justice Building and United States District Courthouse, this 20th day of August, 1998.

JAMES LAWRENCE KING
U.S. DISTRICT JUDGE
SOUTHERN DISTRICT OF
FLORIDA

Case No. 97-2439 CIV-KING

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

NATIONAL FIRE INSURANCE COMPANY
OF HARTFORD, a Connecticut corporation.
Plaintiff,

V.

FORTUNE CONSTRUCTION COMPANY.
A Florida corporation,

V.

ARKIN CONSTRUCTION COMPANY, INC.
Third Party Defendant.

National Fire's First Motion For Partial
Summary Judgment
(Payment Bond Equitable Subrogation)

Plaintiff, National Fire Insurance Company of Hartford ("National Fire"), pursuant to Rule 56 of the Federal Rules of Civil Procedure and Local Rule 7.5, moves for the entry of partial summary judgment against defendant, Fortune Construction Company ("Fortune") establishing that, under the doctrine of equitable subrogation and Florida law: (1) National Fire has a right to recoup payments it made under two specific payment bonds out of the respective contract balances, and (2) this right is superior to Fortune's right to apply those contract balances to claims it may have against the defaulted subcontractor. In support of this motion, National Fire states:

1. This litigation involves two projects to construct residential apartments known as "West Brickell Apartments" ("West Brickell") and "Tract G at Winston Park" ("Winston Park"). Fortune was the general contractor. Affidavit of Raymond M. Lemming, ¶4. (hereinafter "Lemming Affidavit"). Fortune is an affiliate of the owner, the Related Group. Lemming Affidavit, ¶4. Arkin Construction Company, Inc. ("Arkin") was a subcontractor which performed most of the construction activity. Lemming Affidavit ¶4. However, Arkin did not complete its subcontracts. Lemming Affidavit ¶14. Fortune declared Arkin in default. 6/12/97 correspondence from Scott Pestco to Robert Arkin, (attached to the Lemming Aftidavit). Arkin is now a dissolved corporation. Arkin's Answer, ¶2. Both subcontracts have been completed by Fortune. These facts are undisputed.

2. National Fire issued four separate and distinct bonds that are relevant to this lawsuit; (1) a payment bond for Winston Park; (2) a payment bond for West Brickell; (3) a performance bond for Winston Park, and; (4) a performance bond for West Brickell. These four bonds each name Arkin as the principal and Fortune as the obligee. Fn1

3. Each of these four bonds is a distinct and independent contract. Payment and performance bonds secure different obligations. A payment bond provides that the surety shall make payment to subcontractors, laborers and/or materials suppliers that are not paid by the principal. A payment bond protects the owner from mechanics liens by insuring that laborers, subcontractors, and materialmen are compensated for their goods and services by the surety should the contractor default on its payment obligations. A performance bond is a completely different and separate

animal. A performance bond is conditioned upon the principal's faithful and complete performance of the contract. If the principal fails to complete the contract, the surety is liable for the excess costs of completion over the remaining contract balance.

4. This motion is based upon, and limited to, the rights and obligations arising from the two payment bonds. It is not intended to touch upon issues related to the two performance bonds. Fn 2 This motion is solely intended to resolve legal disputes regarding rights and obligations under the payment bonds.

5. The following facts, which are relevant to the resolution of this motion, are undisputed. Fn 3

a. National Fire paid $1,207,466.97 to payment bond claimants under the Winston Park payment bond. Lemming Affidavit ¶15.

b. National Fire paid $225,988.83 to payment bond claimants under the West Brickell payment bond. Lemming Affidavit ¶16.

c. The Winston Park subcontract price, adjusted for change orders, iS $10,899,975.00. Lemming Affidavit ¶12. Arkin was paid $8,709,728.80 for work done before default. Lemming Affidavit ¶12. The difference is $2,190,246.20 (the "Winston Park contract balance"). Lemming Affidavit ¶12.

d. The West Brickell subcontract price, adjusted for change orders, is $4,740,754.39, Lemming Affidavit ¶12. Arkin was paid $4,304,627.55 for work done before default. Lemming Affidavit, 1112. The difference is $436,126.84 (the "West Brickell contract balance"). Lemming Affidavit, ¶12.

e. Fortune has claims against Arkin on the Winston Park project (for liquidated damages and backeharges) that it contends are in excess of the Winston Park contract balance.

f. Fortune has claims against Arkin on the West Brickell project (for liquidated damages and backcharges) that it contends are in excess of the West Brickell contract balance.

6. National Fire contends that it is entitled to the contract balances to recoup its payments. Fortune contends that it is entitled to the contract balances to offset its claims against Arkin. The question of which party has a superior right to the contract balances is a legal question. It is resolved under Florida law by the application of the doctrine of equitable subrogation.

7. Equitable subrogation provides that when a subcontractor fails to pay subsubeomitractors, laborers or materials suppliers, and the surety cures the default by paying off the subsubeontractors, materialmen or laborers, the surety is entitled to recoup its payments out of the unpaid contract balances held by the owner. The surety has priority, to the extent of its payments, over the obligee to the contract balances. The obligee has no right to offset against the surety any claims that it may have against the principal.

8. There is no genuine issue as to any material fact. National Fire is entitled to partial summary judgment as a matter of law.

WHEREFORE, National Fire respectfully requests the Court enter a partial summary judgment in favor of National Fire for $1,433,455.80 (representing the amount paid by National Fire on payment bond claims within

the contract balances) because (1) National Fire has a right to recoup payments it made pursuant to its West Brickell and Winston Park payment bond obligations out of the respective contract balances, and (2) this right is superior to Fortune's right to apply those contract balances to claims it may have against Arkin.

Memorandum of Law

I. The Doctrine of Equitable and its Application to the Instant Facts.

The doctrine of equitable subrogation is "a legal fiction which arises by operation of law where one having a liability, a right, or a fiduciary relationship pays a debt owed by another under circumstances in which he is in equity entitled to the security or obligation held by the creditor whom he has paid." In re Eeaster Marine Inc., 104 B.R. 421, 423 (Bankr.N.D.Fla. 1989). See also, Dixie Nat'l Bank vl Employers Commerial Union Ins. Co. of America, 463 So. 2d 1147 (Fla. 1985). Equitable subrogation arises from law, not from the provisions of a contract. Transamerica Insurance Co. v. Barnett Bank of Marion County, 540 So. 2d 113 (Fla. 1989). It is enforced for the purpose of accomplishing the ends of substantial justice. Pearlman v. Reliance Insurance Co., 371 U.S. 132 (1962).

Equitable subrogation assures that when a contractor fails to pay for equipment or materials and the surety cures the default by paying off the materiairnen and laborers, the surety recoups its payments out of the unpaid contract balances held by the owner. Transamerica, 540 So. 2d at 115116; Pearlman, 371 U.S. at 138-139. The historical benchmark decision that firmly rooted this doctrine iq our juxispnxdcnce is Henningsen v. United States Fidelity & Guaranty Co.,

208 U.S. 404 (1908). In that case, a surety that paid claims of laborers and materialmen upon a contractor's default was held to have an equity in amounts due under the contract superior to that of a bank which received an assignment of contract proceeds to secure a loan to the contractor.

More recently, in Pearlman v. Reliance Insurance Co., 371 U.S. 132 (i962), the Supreme Court followed the now "firmly established rule" that a surety which pays laborers and materialmen is equitably subrogated to the contract balance. Pearlman, 371 U.S. at 141 The court went so far as to state that "probably there are few doctrines better established" than the equitable subrogation rights of the surety which are "widely applied in this country." Pearlman, 371 U.S. at 136-137. This statement was quoted with approval by the Florida Supreme Court in Transamerica Insurance Company v. Barnett Bank of Marion County, 540 So. 2d 113 (Ha.. 1989).

Transamerica is one of many cases that demonstrates the rule that through equitable subrogation, the surety has a priority to the extent of its payments, over everyone (i.e., the obligee, banks, contractors, owners, UCC security interests, the principal's bankruptcy estate, etc.). Transamerica, 540 So. 2dat 116-117 (surety has priority over obligee and bank); Pearlman, 371 U.S. at 141 (surety has priority over principal's bankruptcy estate); In re Ward Land Clearing & Drainage. Inc. 73 B.R. 313 (Bankr.N.D.Fla. l987)(surety has priority over secured creditor, bank and owner); National Fire and Insurance Company of Hartford v. Padula Construction Company, Inc., 118 B.R. 143 (Bankr.S.D.Fla 1990)(surety has priority over owner, obligee, and contractor); Trinity Universal Insurance Co. v. United States, 382 F.2d 317 (5th Cir. 1967)(surety has priority over federal tax lien),

Stated figuratively, a surety's equitable subrogation rights are not limited to those obtained by stepping in the shoes of the defaulting contractor, but the rights extend to those obtained by stepping in the shoes of laborers and materialmen who have been paid by the surety and most importantly, into the shoes of the obligee itself. Transamerica, 540 So. 2d at 115-116; In re Eastern Marine Inc. 104 E.R. 42! (Bankr.N.D.Fla. 1989); In re Ward Land Clearing & 73 B.R. 313 (Bankr.N.D.Fla. 1987).

Of particular relevance to the instant case, it is beyond dispute that a surety's equitable subrogation rights to the contract balance are superior to the right of the obligee (Fortune) to keep these finds. As expressed by the Florida Supreme Court:

> A surety who performs or pays on behalf of an obligee steps into the shoes of the obligee to the extent of performance or payment. . . These rights of the surety as subrogee are not inferior even to the rights of the obligee and may be asserted against the obligee ... . . it is appropriate to give priority to the claims of the surety, up to the limits of its performance.

Transamerica, 540 So. 2d at 116 - 117 citing Pealman v. Reliance Ins. Co., 371 U.S. 132 (1962).

Stated differently, the obligee has no right to "offset" against the surety any claims that it may have against the principal. Caddie Construction Co. Inc. v. Genson 125 B.R. 674, 678 (M.D.Fla. 1991); Aetna Casualty and Surety Co. v. United States, 435 F.2d 1082 (5th Cit. 1970); In re Padula Construction Co. Inc. 118 B.R. 143 (Bankr.S.D.Fla. 1990). This was expressed in a Federal

Court opinion from this district as follows:

> Federal cases are in accord with state law, They uniformly demonstrate that when a surety pays claims or completes ajob or both, its rights to the contract proceeds are superior to the owner's right of offset, even where the owner may have independent claims against the contractor arising from other circumstances.

Padula, 118 B.R. at 145-146. In Padula, the surety (National Fire) asserted that, pursuant to its payment bond obligations, it had paid subcontractors and materialmen of its defaulted principal (a general contractor). Padula, 118 B.R. at 144. National Fire then asserted, as in the instant case, a superior right to the contract proceeds under the doctrine of equitable subrogation. Padula, 118 B.R. at 144. The owner asserted that it had various offsets against the defaulted principal, and that it had suffered damages by reason of the principal's default. Padula, 118 B.R. at 145. National Fire prevailed, as its right to equitable subrogation of the contract balance is superior to the owner's right of offset. Padula, 118 BR. at 145-146. The instant case is indistinguishable.

Under Florida law, the same piles as to subrogation and priority to contract balances exist regardless of whether a surety performs the completion of the project (under a performance bond) or pays laborers and materialmen (payment bond claimants). Transamerca, 540 So. 2d at 116; Padula, 118 B.R. at 145 - 146. The Padula court even stated that Federal cases are in accord with Florida state law and are uniform in denying owners a right of offset in either circumstance. Padula, 118 B.R. at 145-

146. This is true. However, there are a few cases from other jurisdictions that are not in accord. National Fire anticipates that Fortune may use these foreign cases to argue that there should exist a distinction between the obligee's right to offset when the surety's equitable subrogation rights arise from payment bond claims, rather than from the fulfillment of performance bond obligations. As National Fire anticipates that it may not have the opportunity to submit a reply brief before the court rules on this motion, it seems prudent to address these foreign cases that are contrary to Padula (Southern District opinion) and Transamerica (Florida Supreme Court opinion) at this time.

The unfortunate confusion in the law of otherjurisdictions arises out of the Supreme Court's somewhat obtuse opinion in United States v. Munsey Trust Co., 332 U.S. 234 (1947). In Munsey, a surety paid payment bondclaims on a United States government public project and sought to recover the contract balances. Munsey, 332 U.S. at 236. The government's position was that it had a superior right to first reduce the contract balance due to a liquidated claim against the contractor arising from another project. Munsey, 332 U.S at 238. In essence, the government was seeking to offset an independent claim against the contractor arising from other circumstances - exactly what Psfuls holds is improper. However, the Munsey court held for the federal government in an opinion that is not a model of clarity.

For a time, it was believed by some courts and scholars that Munsey had overruled Henningsen and its companion case, Prairie State Bank v. United States, 164 U.S. 227 (1896). This belief was firmly rejected by the Supreme Court in Pearlman, as follows:

> The [Munsey] opinion contained statements which some have interpreted as meaning that we were abandoning the established legal and equitable principles of the Prairie Bank arid Henningsen cases under which sureties can indemnify themselves against losses. But the equitable rights of a surety declared in the Prairie Bank case as to sureties who complete performance of a contract were expressly recognized and approved in Munsey, and the Henningsen rule as to sureties who had not completed the contract but had paid laborers was not mentioned. Henningsen was not even cited by the Munsey opinion. We hold that Munsey left the rule in Prairie Bank and Henningsen undisturbed. We cannot say that such a firmly established rule was so casually overruled.

Pearlman, 371 U.S. at 140-141. However, it remained unclear how Munsey and Pearlman should be reconciled. There are three schools of thought on this question: (1) Pearlman overruled Munsey altogether; (2) Munsey is limited to cases where the United States (rather than a private entity) is seeking to offset flmds, and; (3) Munsey is limited to payment bond, rather than performance bond claims, regardless of whether the United States is the obligee. See for discussion of these three schools of thought, Universal Bonding Insurance Co. v. Gittens and Sprinke Enterprises, Inc., 960 F.2d 366 (3d Cir. 1992)(a recent discussion); United States Fidelity & Guaranty Co. v. United States, 475 F.2d 1377 (Ct.Cl. 1973)(a definitive and influential court of claims case); Glassman Construction Co. v. Fidelity and Casulty Co., 356 F.2d 340 (1966)(representative of

earlier judicial struggles to reconcile these cases).

National Fire prevails on this motion under the first two schools of thought. National Fire anticipates that Fortune may present cases following the third school of thought. However, that requires a strained interpretation of Munsey. The more sensible interpretation of Munsey is that the result was arrived at because the United States was the entity attempting to assert an offset. At the time that Munsey was decided, laborers and materialmen could not have an enforceable right against the United Stated due to the rule that they cannot acquire a lien on public buildings or a right to government held funds. Munsey 332 U.S. at 241. Thus, the surety could not recover by standing in the shoes of the laborers and materialmen, because their "shoes" were impotent to recover against the federal government. Munsey, 332 U.S. at 242. Similarly, the surety could not stand in the shoes of the obligee (the government) because the surety was not paying a debt that the government could otherwise be held liable to pay. Munsey, 332 U.S. at 242.

Florida courts have uniformly and overwhelmingly rejected the third school of thought in favor of the second school of thought - thus requiring National Fire to prevail on this motion under Florida law. The only case from a state court in Florida to address Munsey interpreted its holding to be based upon the fact that the United States was the entity asserting the offset - thus adopting the second school of thought and rejecting the third school of thought. Transamerica Insurance Company v. Barnett Bank of Marion County, 524 So. 2d 439 (Fla. 5th DCA 1988) overruled on other grounds 540 So. 2d 113. Two Federal Courts in Florida have also interpreted the critical distinguishing feature of Munsey to be that the federal government was the entity that

sought to apply the offset. Mount Sinai Hospital of Greater Miami v. Weinberger, 517 F.2d 329 (5th Cit. (Fla) 1975); In the Matter of Bruce Construction Corp., 217 F.Supp. 926 (S.D.Fla. 1963). The only other Florida cases that have cited Munsey did so to enforce a claim of the federal government. See, United States v. Owens, 329 F.2d 678 (5th Cir. 1964); Lawyers' Title Guaranty Fund v. United States, 508 F.2d 1 (5th Cir. 1915); Capuano v. United States, 955 F.2d 1427 (11th Cir. 1992).

Most importantly, the Florida Supreme Court and a Federal Court of this District have both held that the obligee has no right of offset regardless of whether the surety is paying under a payment bond or performing under a performance bond, thus implicitly rejecting the "third school of thought." Transamerica, 540 So. 2d at 116 - 117; Padula, 118 B.R. at 145-146. This is the correct rule. This court should not be influenced by an argument to the contrary that is based upon a strained interpretation of Munsey from the case-law of other jurisdictions.

II. Summary Judgment is Appropriate.

Summary judgment is proper "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed.R.Civ.P. 56(c). The burden is on the moving party to demonstrate the absence of a genuine issue of material fact. Keiser v. Coliseum Properties Inc., 614 F.2d 406 (5th Cir. (Fla.) 1980). This burden may be discharged by showing that there is an absence of evidence to support the non-moving party's case. Employers Insurance of Wausan v. Able Green Inc., 749 F.Supp. 1100 (S.D.Fla. 1990). The burden. then shifts to

the non-moving party to go beyond the pleadings and designate specific facts showing that there is a genuine issue for trial. De Cuellar v. Brady 881 F.2d 1561 (11th Cir. (Fla.) 1989).

One purpose of summary judgment is to isolate, and then terminate, defenses that are factually unsupported or improper as a matter of law. Celotex v. Catrett, 477 U.S. 317 (1986). The Supreme Court has emphasized that summary judgment is to be viewed not as a disfavored technical shortcut, but rather as an integral component of the Federal Rules. Id., 477 U.S. at 327. Summary judgment motions must be resolved not only with an appropriate regard for the rights of defendants to have their positions ruled upon by a factfinder, but also with due regard for the rights of persons opposing such defenses to demonstrate, before trial, that the defenses have no factual basis or are improper as a matter of law. Id., 477 U.S. at 327.

In the instant case, it is a pure legal question whether: (1) National Fire has a right to recoup payments it made under two specific payment bonds out of the respective contract balances, and (2) this right is superior to Fortune's right to apply those contract balances to claims it may have against the defaulted subcontractor. On a motion for partial summary judgment, the Court may summarily resolve individual issues as to which there exist no genuine issue of material fact. Fed.R.Civ.P. 56(d). This serves the judicial process by accelerating litigation and narrowing the triable issues. Antenor v. D & S Farms, 866 F.Supp. 1389 (S.D.Fla. 1994), overruled on other grounds, 80 F. 30-925 (11th Cir. (Fla.) 1996).

Finally, it should be understood that motion for partial summary judgment is directed solely to rights and

obligations arising under the two payment bonds. A bond is a contract. American Home Assurance Co. v. Larkin General Hospital Ltd., 593 So. 2d 195 (Fla. 1992). Therefore, a bond is subject to the general law of contracts. Larkin, 593 So. 2d at 197. Under the general law of contracts, where an obligation arises under a contract, the party owing that obligation may not avoid the obligation by claiming that the other party has breached a different contract. Ja Dan Inc. v. L - J Inc., 898 F.Supp. 894 (S.D.Fla. 1995); Dickerson Inc. v. F.D.I.C., 244 So. 2d 748 (1st DCA 1971); B & V Limited v. All Dade General Construction Inc., 662 So. 24413 (Fla. 3d DCA 1995). Fn 4 This is not to say that the party owing the obligation may not assert (and potentially recover for) the breach of the other contract as a counterclaim or separate action. B & V Limited, 662 So. 2d 413 (Fla. 3d DCA 1995). However, the contracts must be considered individually - even if other distinct contracts (i.e., performance bonds) are allegedly breached, that does not provide an excuse to avoid obligations arising under these contracts (i.e., payment bonds). This motion for summary judgment stands or falls solely on the payment bonds.

Conclusion

National Fire is entitled to entry of partial summary judgment in its favor for $1,433,455.80 (representing the amount paid by National Fire on payment bond claims within the contract balances) because (1) National Fire has a right to recoup payments it made pursuant to its West Brickell and Winston Park payment bond obligations out of the respective contract balances, and (2) this right is superior to Fortune's right to apply those contract balances to claims it may have against Arkin.

FILED
JUL 29 2003
OFFICE OF THE CLERK

No. 03-12

IN THE

Supreme Court of the United States

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD,

Petitioner,

v.

FORTUNE CONSTRUCTION COMPANY,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTION PRESENTED FOR REVIEW

Whether the decision of the Eleventh Circuit Court of Appeals presents no basis for review because it simply applied established Florida law based on the terms of Petitioner's performance bonds to the facts and circumstances of this particular case, and did so in a manner that is consistent with the decision of the Fifth Circuit as to which Petitioner asserts conflict.

STATEMENT PURSUANT TO RULE 29.6

Fortune Construction Company is a General Partnership.

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Appendix B — Answer And Affirmative Defenses Of Fortune Construction Co. Dated August 20, 1997 Filed In The United States District Court For The Southern District Of Florida 12a

STATEMENT OF THE CASE

A. Reply to Petitioner's Statement of the Case

Petitioner's brief contains misstatements of fact and law, identified below, in accordance with Rule 15(2).[1] Respondent also notes that Petitioner's Appendix contains only the decisions and orders of the district court and of the Eleventh Circuit, and Respondent therefore relies upon the Petitioner's Appendix as containing the only materials upon which Petitioner relies as essential to the Court's understanding of the Petition. Rule 14(1)(i)(v). Petitioner's brief, however, contains almost no Appendix references to support its factual recitations, and many of its factual recitations are not supported by anything in the Petitioner's Appendix.

Neither has Petitioner included any recital of the terms of the surety bonds and construction contracts upon which its question presented for review by this Court is based. Respondent respectfully submits that these deficiencies in the Petition – which also hinder Respondent's ability to respond – are sufficient basis for the denial of the Petition without more. Rule 14(4).

Respondent also believes, however, that the facts material to the determination of whether this case presents any basis for exercise of this Court's jurisdiction are few and undisputed. All such facts appear on the face of the Eleventh Circuit's decision, which is included in the Petitioner's Appendix, at pages 1 through 38. Respondent accordingly presents a brief statement of the case with

1. Respondent makes reference to the Rules of the Supreme Court of the United States herein as "Rule __."

Appendix references to the undisputed material facts as recited in the Eleventh Circuit's decision.

B. Respondent's Statement of the Case

1. The undisputed material facts

The question presented in the Petition arises out of the Eleventh Circuit's decision as to the duties and obligations owed by Petitioner National Fire Insurance Company pursuant to certain performance and payment bonds issued by Petitioner in connection with two apartment complex construction projects in South Florida, known as the Winston Park and West Brickell projects. (Petitioner's Appendix, p. 2).[2] Respondent Fortune Construction Company was the general contractor on the projects and Arkin Construction Company was its subcontractor. (Petitioner's Appendix, p. 2). Arkin obtained the National Fire surety bonds to secure Arkin's payment and performance obligations under its subcontracts for the projects. (Petitioner's Appendix, p. 2).

The Winston Park project payment and performance bonds were selected by National Fire from standard industry forms, while the West Brickell project payment and performance bonds were separately drafted by National Fire. (Petitioner's Appendix, p. 2). Each of the performance bonds and each of the payment bonds, however, specifically "incorporated the appropriate subcontract between Fortune and Arkin by reference." (Petitioner's Appendix, p. 2).

---

2. References to the Petitioner's Appendix appear as (Petitioner's Appendix, p. __). Respondent has also provided an Appendix with this brief, which is referenced as (Respondent's Appendix, p. __).

The ***pivotal fact*** for purposes of this Court's determination of the question presented for review is undisputed, and was stated in the Eleventh Circuit's decision as follows: "The construction subcontracts [between Fortune and Arkin] each contained a clause obligating Arkin to pay liquidated damages for delays in completing the projects." (Petitioner's Appendix, p. 3). Specifically, as the Eleventh Circuit also noted: "The Winston Park Subcontract provided for liquidated damages of $35 per day per incomplete apartment and $1,000 per day for incomplete common areas. The West Brickell Subcontract provided for liquidated damages after a specified date of $30 per day per incomplete apartment." (Petitioner's Appendix, p. 3).

Arkin began experiencing financial difficulties while working on the two projects, and failed to meet various payment obligations to subcontractors and suppliers. (Petitioner's Appendix, p. 2). Delays ensued, and Arkin eventually abandoned the project altogether. (Petitioner's Appendix, pp. 2-3). Fortune initially tried to work through the problems with Arkin, but declared Arkin in default when Arkin abandoned the projects. (Petitioner's Appendix, pp. 2-3). Fortune notified National Fire of Arkin's default, and demanded that National Fire perform its obligations under the performance bonds for completion of Arkin's work on the projects. (Petitioner's Appendix, p. 3). National Fire did not complete either project despite demand, and Fortune was compelled to perform the subcontracts. (Petitioner's Appendix, p. 3).

2. The litigation over the obligations and entitlements created by the subcontractor's defaults

Litigation thereafter ensued between National Fire, Fortune, and Arkin over a variety of issues, including National Fire's asserted subrogation rights for having paid some of the subcontractors and suppliers under the payment bonds, Fortune's asserted rights to damages from Arkin for breach of the construction subcontracts, Fortune's asserted rights to recover for National Fire's breach of the performance bond, and the priorities amongst the parties' rights to funds held by Fortune consisting of the amount left from the contract price after completion of the projects. (Petitioner's Appendix, pp. 3-5). The litigation was initiated by National Fire in the federal district court for the Southern District of Florida on the basis of that court's diversity jurisdiction. (Petition, p. 3).

The only issue here is Fortune's claim for the liquidated delay damage amount that was owed to Fortune under the terms of its subcontract with Arkin. (See Petition, p. i, "Questions Presented for Review"). Fortune contended that because National Fire's performance bonds specifically incorporated the terms of the Arkin subcontracts by reference, and since the Arkin subcontract contained a specific clause obligating Arkin to pay liquidated damages for delays in completing the projects, Fortune was entitled to recover the liquidated delay damage amount from National Fire. (Petitioner's Appendix, p. 20). National Fire's position was presented in a complex manner – via seven different motions for partial summary judgment – making various arguments over the priorities of rights and obligations amongst the three

parties. (Petitioner's Appendix, p. 5).[3] The argument made by National Fire that is pertinent here was that despite the fact that its performance bonds incorporated the Arkin subcontracts by reference, it should not have to pay the liquidated delay damage amounts owed under the Arkin subcontracts because the bonds did not say *on their face* that they would cover delay damage amounts. (Petitioner's Appendix, p. 21).

3. The Eleventh Circuit's decision

The Eleventh Circuit correctly noted that it would be bound to follow Florida law in deciding the issue in this diversity case, and therefore "look[ed] to Florida law to see what a surety's obligations are in the circumstances of this case." (Petitioner's Appendix, p. 21). The Eleventh Circuit then determined that it should follow the Florida Supreme Court's decision in *American Home Assurance Co. v. Larkin General Hospital, Ltd.*, 593 So. 2d 195 (Fla. 1992). The *Larkin* Court had decided, based on the unremarkable proposition that "[a] bond is a contract, and therefore, is subject to the general law of contracts", 593 So. 2d at 197, that "[t]he language in the performance bond, construed together with the purpose of the bond" determines the liability of the surety under the bond. *Id.* at 198. (Petitioner's Appendix, p. 22). The bond in *Larkin* did not include any language that specifically provided for payment of delay damages, and the *Larkin* Court held that *for that reason* the surety would not be liable for delay damages. (Petitioner's Appendix, pp. 21-22).

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3. As the Eleventh Circuit pointed out: "National Fire's attempt to break this case into little pieces seems to have contributed to the confusion below." (Petitioner's Appendix, p. 31).

The Eleventh Circuit noted the critical factual distinction between the *Larkin* facts and those presented here: ***"Importantly for purposes of our analysis, there was no liquidated or other type of damages provision in the underlying contract."*** (Petitioner's Appendix, p. 21) (emphasis added). The Eleventh Circuit then went on to apply the principle enunciated in *Larkin,* i.e., that a surety will not be liable for delay damages unless its bond contract language specifically provides coverage for delay damages, to the facts and circumstances presented in the instant case with the following discussion:

The *Larkin General Hospital* court noted:

> [t]he purpose of a performance bond is to guarantee the completion of the contract upon default by the contractor. Ordinarily a performance bond only ensures the completion of the contract. The surety agrees to complete the construction or to pay the obligee the reasonable costs of completion if the contractor defaults.

Id. at 198 (citations omitted). Although a surety's liability is coextensive with that of the principal, "the surety's liability for damages is limited by the terms of the bond." *Id.* Therefore, the Supreme Court of Florida found that "[t]he language in the performance bond, construed together with the purpose of the bond, clearly explains that the performance bond merely guaranteed the completion of the construction contract and nothing more." *Id.* (emphasis added); *see also*

> *Mycon Constr. Corp. v. Board of Regents*, 755 So.2d 154, 155 ([Fla.] 4th DCA 2000) ("Because the performance bond contains no provision for damages for delay, the surety cannot be held liable for such damages."). ***However, unlike the performance bond in Larkin General Hospital, the bonds at issue in this case expressly incorporated the subcontracts, which, in turn, do expressly provide for liquidated delay damages.***

(Petitioner's Appendix, pp. 21-22) (emphasis added). The Eleventh Circuit then went on to discuss the argument advanced by Petitioner National Fire here, i.e., that *Larkin* should be read to require the provision for payment of liquidated delay damages to appear on the face of the bond in order to be enforceable against the surety. (Petitioner's Appendix, pp. 22-23). The Eleventh Circuit rejected that interpretation because it would disregard the *Larkin* holding that the surety's obligation is to be determined from the language and *purpose* of the bond, as well as established contract principles as to incorporation by reference, which *are* applied in surety bond cases, notwithstanding Petitioner's implications to the contrary:

> *Larkin General Hospital* could possibly be interpreted to mean that a performance bond surety cannot be held liable for, or denied subrogation for, delay damages, whether liquidated or unliquidated, unless the responsibility for delay damages is specified on the face of the performance bond. However, we

do not read the decision that broadly.[4] ***The "purpose of the bond" must be considered, which requires reference to the contract secured by the bond. Where a provision for liquidated delay damages is clearly delineated in the underlying contract and incorporated by reference into the bond, the surety is on notice of the time element of performance and the contractual consequences of failure to timely perform in accordance with the contract.*** Once the liquidated damages accrue, the contractor-principal owes a debt to the obligee which is, in effect, a reduction of (or contractual off-set to) the contract price. In such event, the obligee becomes the creditor of the principal and the performance bond surety should not have superior rights to the obligee in the remaining contract balances where liquidated damages have been suffered. ***This is especially true where, as here, the surety does not remedy the principal's delay by performing the surety's obligations under the performance bond.***

While it is true that the terms of the bonds in this case do not expressly require the surety to assume responsibility for delay, "[i]t is the general rule of contract law that where a writing expressly refers to and sufficiently describes another document, the other document is to be interpreted as part of the writing." *Lord & Son*

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4. The Eleventh Circuit expressly recognized in its opinion that the Florida Supreme Court's decision in *Federal Ins. Co. v. Southwest Fla. Retirement Ctr.*, 707 So. 2d 1119, 1121 (Fla.1998) thereafter declined to extend *Larkin General Hospital* beyond delay damages. (Petitioner's Appendix, p. 21).

> *Constr., Inc. v. Roberts Electrical Contractors, Inc.*, 624 So.2d 376, 377 n. 2 (Fla. 1st DCA 1993). Even after *Larkin General Hospital*, Florida courts have continued to utilize the well-established doctrine of incorporation by reference to impose liability on a performance bond surety. *See DCC Constructors, Inc. v. Randall Mech. Inc.*, 791 So.2d 575, 576-77 (Fla. 5th DCA 2001); *Southwest Fla. Retirement Ctr. v. Fed Ins. Co.*, 682 So.2d 1130, 1132-33 (Fla. 2d DCA 1996), *aff'd*, 707 So.2d 1119 (Fla.1998). The "purpose" of the performance bonds was to insure performance in accordance with the terms of the respective subcontracts, and those terms plainly include adverse direct consequences for delay. ***Therefore, under the particular facts of this case, the unequivocal delay damages provisions of the subcontracts are properly considered part of the bonds issued by National Fire because of the incorporation by reference.***

(Petitioner's Appendix, pp. 23-24). Based on the above stated reasoning, the Eleventh Circuit concluded that Fortune was entitled to the right to seek recovery of contractually mandated liquidated delay damages from National Fire. (Petitioner's Appendix, p. 24).

4. Petitioner's claimed conflict

Petitioner contends that the Eleventh Circuit's decision creates conflict with the Fifth Circuit's decision in *L & A Contracting Co. v. Southern Concrete Services*, 17 F.3d 106 (5th Cir. 1994). Specifically, Petitioner argues that the Eleventh Circuit interprets *Larkin* differently than did the

Fifth Circuit in *L & A Contracting*. *L & A Contracting*, however, did not involve a bond that incorporated by reference a subcontract with a specific provision for liquidated delay damages. In fact, the entire discussion in *L & A Contracting* of *Larkin* and of a surety's liability for delay damages was as follows:

> F & D [the surety] next challenges the district court's judgment holding it liable for delay damages. We need not linger long on this question because it is directly controlled by the Florida Supreme Court's opinion in *American Home Assurance Co. v. Larkin General Hospital, Ltd.* The *Larkin* Court held that "the surety's liability for damages is limited by the terms of the bond". The bond here contained no provision imposing liability on F & D for delay damages, and the district court may not imply such a provision. Therefore, the district court erred in holding F & D liable for delay damages.

17 F.3d at 112. The Eleventh Circuit's decision here does not conflict in any way with the *L & A Contracting* Court's few remarks on the extent of performance bond liability for delay damages. The Eleventh Circuit certainly did not 'imply' a delay damage provision where no such provision existed under the bonds' language. National Fire's own performance bonds each incorporated delay damage provisions by reference.

REASONS FOR DENYING THE PETITION

Petitioner contends that conflict between Circuits has been created as to an important matter and/or that the Eleventh Circuit has so far departed from the accepted and usual course of judicial proceedings as to call for exercise of this Court's supervisory powers. Respondent submits that neither circumstance is presented here, and that jurisdiction should accordingly be declined. Respondent also submits that misstatements of law and fact in Petitioner's brief present a further basis for denial of the request for a writ under Rule 14(4).

I. NO CONFLICT IS PRESENTED

The subject Eleventh Circuit decision, the Fifth Circuit's decision in *L & A Contracting,* and the Florida Supreme Court's decision in *Larkin* all stand for precisely the same propositions of law. All of the cases are in agreement that: (1) a surety bond is a contract and therefore subject to the general law of contracts; (2) a surety bond must accordingly be construed in accordance with its language and purpose; and (3) under these contract principles of construction, a surety bond will not be held to cover delay damages unless the contracting language of the bond specifically so provides.

As set out in the Eleventh Circuit's decision in this case, Petitioner's performance bonds here specifically incorporated the terms of the Arkin subcontracts by reference, and the subcontracts contained very specific liquidated delay damage provisions. The bonds here were accordingly held to cover the liquidated delay damage amounts.

The bonds in *L & A Contracting* and *Larkin* did *not* contain contracting language that incorporated by reference specific liquidated delay damage terms of the subcontracts, and the bonds in those cases were held not to cover delay damages for that reason. The Eleventh Circuit's decision here merely applies the law established in *Larkin* to a different set of facts then those presented in *L & A Contracting*. No conflict whatsoever has been created.

II. THE SUBJECT DECISION HAS NO NEW RAMIFICATIONS FOR THE SURETY INDUSTRY

Petitioner also advances the alarmist argument that the Eleventh Circuit's decision will place the entire surety industry in jeopardy by making it liable for delay damages never contemplated by the industry. This argument has neither factual nor legal support.

The Eleventh Circuit has merely reiterated the unexceptional principle that sureties will be obligated to the extent of the contract language in their bonds - neither more nor less. And, while sureties *may* use some of the standard forms developed by the industry, they are certainly not required to do so. Each surety is the master of its own fate in that regard, and thus has control over the extent of its obligations under its bonds. Petitioner National Fire here, for example, used standard form bonds for one of the projects, and drafted its own forms for the other. (Petitioner's Appendix, p. 2).

Furthermore, the fact that some performance bonds are held to cover actual and liquidated delay damages has long been known to the surety industry, not least from reported case law spanning many decades. *See, e.g., Continental*

Realty Corp. v. Andrew J. Crevolin Co., 380 F. Supp. 246 (S. D.W. Va. 1974) (surety that failed to perform under performance bond could be held liable for damages caused by delay, even where delay damage amounts exceeded the maximum penalty amount set by the bond); *Southern Roofing & Petroleum Co. v. Aetna Insurance Co.*, 293 F. Supp. 725 (E.D. Tenn. 1968) (surety was liable for ten percent liquidated delay damage penalty provided for in subcontract where bond specifically incorporated the subcontract's terms by reference); *New Amsterdam Casualty Company v. Mitchell*, 325 F.2d 474 (5th Cir. 1964) (surety on contractor's performance bond held liable for delay damages consisting of additional interest on construction loan occasioned by delay); *Miracle Mile Shopping Center v. National Union Indemnity Company*, 299 F.2d 780 (7th Cir. 1962) (surety held liable for delay damages caused by contractor's default and surety's failure to take over construction or pay for completion); *Mason* v. *City of Albertville*, 158 So. 2d 924 (Ala. 1963) (liquidated damages representing $100 per day for overrun of 381 days in completing sewer construction contract was a loss suffered under contract by obligee of contractor's performance bond, and such loss was covered by bond); *Industrial Indemnity Co. v. Wick Construction Co.*, 680 P.2d 1100 (Alaska 1984) (surety on performance bond held liable along with subcontractor for delay damages under liquidated delay damage provision in subcontract); *Cates Construction, Inc. v. Talbot*, 980 P.2d 407 (Cal. 1999) (bond and construction contract construed together to permit developer to recover delay damages from surety); *Pacific Employers Insurance Co. v. City of Berkeley*, 158 Cal. App. 3d 145 (Cal. 1st DCA 1984) (where performance bond incorporated construction contract by reference; surety was bound by contract's provision for liquidated delay damages); *Hemenway Company, Inc. v. Bartex, Inc. of Texas*,

373 So. 2d 1356 (La. 1st Cir. 1979) (surety held liable along with contractor for delay damages for untimely completion of project).

The surety industry has, in short, been aware that bonds may create potential liability for delay damages for more than sufficient time to react in whatever ways the industry deemed prudent, including in the drafting of the language of bonds and in assessing adequate premiums. Neither is there any novelty to the fact that the delay damage liability may be triggered by language in a bond incorporating by reference the terms of an underlying construction contract.

Petitioner has failed to demonstrate that the Eleventh Circuit departed in any way from the accepted and usual course of judicial proceedings with its decision. And, Respondent respectfully submits, Petitioner's suggestion that the Eleventh Circuit's decision "threatens to accidentally devastate the surety industry" (Petition, p. 14) is unsupported rhetoric that does not transform this case into one of exceptional importance calling for exercise of this Court's supervisory powers.

III. MISSTATEMENTS IN THE PETITION

The Petition asserts as a major theme throughout that the Eleventh Circuit did not understand the parties' claims as presented to the district court, and that accordingly the Eleventh Circuit did not have the benefit of briefs on the correct issues. For example, the Petition states at page 6: "As the Eleventh Circuit's opinion is largely devoted to its misunderstanding of the record, it did not have the benefit of briefs on issues that were not part of the record." (Petition, p. 6). The Eleventh Circuit's extremely thorough

opinion contradicts Petitioner's assertions in this regard. But, for present purposes, we note that it is inaccurate for Petitioner to state that the Eleventh Circuit was never given any briefing on these issues that the Petitioner claims the Eleventh Circuit misunderstood. In fact, Petitioner briefed all of the arguments for the Eleventh Circuit in its Amended Petition for Reconsideration, which we have included in an Appendix to this brief. (Respondent's Appendix, pp. 1a-11a).

The Amended Petition for Rehearing shows that Petitioner presented the Eleventh Circuit with briefing on *all* of the issues that the Petition states were never briefed for the Eleventh Circuit. In fact, the arguments in the Amended Petition for Rehearing are repeated almost verbatim in the Petition filed with this Court. It is thus not true that the Eleventh Circuit did not have the benefit of briefing on the issues presented herein.

The Petitioner goes on to state that "the Eleventh Circuit also apparently did not consider the more recent Florida Supreme Court case of *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998)." (Petition, p. 12). In fact, the Eleventh Circuit's decision ***expressly*** acknowledges that case, and accurately notes its holding refusing to extend *Larkin* beyond delay damages. (Petitioner's Appendix, p. 21).

The Petition also states:

> Under the holding of these cases [referring to *Larkin* and *L & A Contracting*], if a performance bond specifies that it incorporates the underlying contract, but it does not specify on its face that the surety is responsible for delay damages arising

> from untimely performance of the underlying contract, liability for delay damages is not imposed on the surety.

(Petition, p. 6). This is clearly a misstatement of the holdings of these cases. As discussed in full above, the cases hold that the coverage of a performance bond will be determined under ordinary contract construction principles. Neither the *Larkin* nor *L & A Contracting* bonds incorporated by reference subcontracts with specific provisions for payment of delay damages, so, under ordinary contract law principles, the *Larkin* and *L & A Contracting* sureties were held to have no liability for delay damages. Neither decision says that liability for delay damage will not be imposed on a surety whose bond incorporates a delay damage provision by reference rather than stating it on the face of the bond.

Finally, the Petition makes the following direct misstatements of fact:

> Next, the Eleventh Circuit ***mistakenly believed that Fortune sought to recover the liquidated delay damages from National Fire in the underlying suit under a theory that they were the responsibility of National Fire under the performance bonds. Such a theory was not pled or otherwise asserted by Fortune before the District Court,*** likely because it was expressly barred by the Florida Supreme Court's holding in Larkin[.] . . . ***To attempt to avoid the holding of Larkin General Hospital , Fortune framed its theory of delay damages as a "set-off" that could***

> ***be applied to Arkin's unpaid contract balances, rather than an affirmative claim for recovery of damages under the performance bond.***

(Petition, pp. 5-6). The fact is that Fortune filed not only an answer and affirmative defenses claiming set-offs, but also a counterclaim which, in Count I, claimed ***precisely*** those damages from National Fire and on ***precisely*** that theory. A copy of Fortune's Answer and Counterclaim have accordingly been included in the Respondent's Appendix hereto. (Respondent's Appendix, pp. 12a-22a). Count I reads, in pertinent portion:

COUNTERCLAIM

* * *

COUNT I

* * *

9. In addition, FORTUNE demanded that NATIONAL FIRE honor its obligations under the Performance Bond attached hereto as Exhibit "B".

10. Despite said demands, NATIONAL FIRE has failed and refused to honor its obligations under the aforesaid surety bond and has breached not only its obligation to remedy the default of its principal, ARKIN, but also its obligation to perform those duties set forth in the bond as surety.

11. By virtue of the aforesaid default by ARKIN, ***as well as the breach of the obligations under***

> ***the Performance Bond by NATIONAL FIRE, Counterclaimant has been damaged.***
>
> 12. ***The damages incurred by Counterclaimant*** are in excess of $15,000 and ***include, but are not limited to, the following which may encompass consequential and/or special damages contemplated by the parties:***
>
> * * *
>
> (e) Impact to other projects, including interest and ***delay expenses;***
>
> * * *
>
> (h) ***Delay damages*** caused by the failure of the surety to perform its obligations[.]

(Respondent's Appendix, pp. 16a-18a).

Further, the Eleventh Circuit's decision confirms that the Eleventh Circuit was well-acquainted with the actual record, and with the fact that Respondent Fortune had raised *both* set-off claims *and* affirmative claims for damages under the performance bond as to the delay damages:

> Fortune contends that National Fire is responsible for liquidated delay damages that had accrued prior to Arkin's default due to Arkin's failure to timely perform on both projects. Although Fortune obtained judgment as a matter of law against Arkin

> for these damages, ***Fortune seeks to set these damages off against the retained contract balances. Fortune also argues that National Fire is contractually liable for these damages because the bonds incorporated by reference the underlying subcontracts which expressly provided for delay damages.***

(Petitioner's Appendix, p. 20).

The foregoing misstatements of law and fact are such that Petitioner has failed to make an accurate presentation as required by Rule 14(4), justifying denial of the Petition on that basis alone.

CONCLUSION

Based on the foregoing facts and authorities, Respondent respectfully submits that the Petitioner's request for a writ of certiorari should be denied.

Respectfully submitted,

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APPENDIX

APPENDIX A — AMENDED PETITION FOR RECONSIDERATION OF NATIONAL FIRE INS. CO. OF HARTFORD DATED MARCH 6, 2003 FILED IN THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

Docket No. 01-15124F

Case No. 97-2439-Civ-King

FORTUNE CONSTRUCTION CO., INC.,

Appellant,

v.

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD,

Appellee,

On Appeal from United States District Court
for the Southern District of Florida

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD'S AMENDED PETITION FOR RECONSIDERATION

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Appendix A

UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

Docket No. 01-15124F

Case No. 97-2439-Civ-King

FORTUNE CONSTRUCTION CO., INC.,

Appellant,

v.

NATIONAL FIRE INSURANCE COMPANY
OF HARTFORD,

Appellee,

On Appeal from United States District Court
for the Southern District of Florida

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD'S AMENDED PETITION FOR RECONSIDERATION

Plaintiff/Appellee, National Fire Insurance Company of Hartford ("National Fire") respectfully petitions for Reconsideration of the Opinion filed February 7, 2003 (the "Opinion"). The grounds for this petition include:

(1) The Parties apparently failed to adequately explain the record of this convoluted case, as the Opinion is largely directed to the issue that "[t]he district court erred to the extent that it granted summary judgment for National Fire

on its claim of equitable subrogation arising out of the performance bonds." The district court did not grant summary judgment for National Fire on a claim of equitable subrogation arising out of the performance bonds. National Fire did not even make such a claim in this case, or bring such a motion, and this issue was not a subject of the appeal.

(2) Perhaps as a result of the Court addressing an issue not contemplated by the parties, and therefore not adequately addressed in the briefs, the Opinion makes an obvious fact error in the manner that it distinguishes the Florida Supreme Court case of *American Home Assurance Co. v. Larkin General Hospital, Ltd.*, 593 So. 2d 195 (Fla. 1992). Specifically, the Opinion turns upon the suggested distinction that the bond in *Larkin General Hospital* did not incorporate the underlying construction contract. However, reported Florida decisions that do set forth the specific terms of the performance bond under consideration in *Larkin General Hospital* show the performance bond to be identical in this regard to the performance bond in the instant case. The Opinion thus turns on this fact error.

(3) Once this incorrect distinction is removed, it is apparent that the "incorporation analysis" applied by the Opinion to expand the liability of a performance bond surety is inconsistent with *Larkin General Hospital* and its progeny, *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998).

(4) The Opinion did not have the benefit of considering a very recent case on-point that was decided and published

after the submission of briefs. This recent authority directly contradicts the Opinion in its interpretation of *Larkin General Hospital* and *Southwest Florida Retirement*.

I. The Holding and Analysis of the Opinion is Misplaced as it Addresses Whether National Fire is Entitled to Equitable Subrogation Arising Out of the Performance Bonds. This was Not an Issue in the Case.

A lengthy portion of the Opinion is devoted to an analysis of whether National Fire was entitled to equitable subrogation rights arising out of the performance bonds. A holding of the Opinion is that "[t]he district court erred to the extent that it granted summary judgment for National Fire on its claim of equitable subrogation arising out of the performance bonds." However, this holding and analysis is misplaced and arises from an apparent misinterpretation of the record. The district court never granted summary judgment for National Fire on a claim of equitable subrogation arising out of the performance bonds. National Fire never moved for summary judgment on a claim of equitable subrogation arising out of the performance bonds. National Fire did not assert such a claim in this case, and indeed, would have no basis for such a claim in this context as it did not expend any funds to complete the work.

The misinterpretation of the record may have arisen because the Order granting National Fire's Motion for Partial Summary Judgment is not a model of clarity. However, the Motion itself, entitled "National Fire's First Motion for

Partial Summary Judgment (Payment Bond Equitable Subrogation)" is clear. Paragraph 4 states as follows:

> This motion is based upon, and limited to, the rights and obligations arising from the two payment bonds. It is not intended to touch upon issues related to the two performance bonds. This motion is solely intended to resolve legal disputes regarding rights and obligations under the payment bonds.

As the question of whether National Fire was entitled to equitable subrogation rights arising out of the performance bonds was not an issue in this case, it should not be a focus of the Opinion. Certainly, the Opinion should not hold that "[t]he district court erred to the extent that it granted summary judgment for National Fire on its claim of equitable subrogation arising out of the performance bonds" when no such grant of summary judgment occurred, and no such claim was asserted.

II. The Opinion Distinguishes *Larkin General Hospital* Based Upon the Incorrect Belief that the Performance Bond in that Case Did Not Incorporate the Contract.

The unnecessary consideration in the Opinion of the issue of whether National Fire had any equitable subrogation rights under the performance bond unfortunately led to an incorrect interpretation of *American Home Assurance Co. v. Larkin General Hospital, Ltd.*, 593 So. 2d 195 (Fla. 1992). The Court did not have the benefit of a thorough briefing on this issue and perhaps as a result mistakenly distinguished *Larkin*

General Hospital in the Opinion as follows: "[h]owever, unlike the performance bond in *Larkin General Hospital*, the bonds at issue in this case expressly incorporated the subcontracts." This is just factually wrong, although it requires a review of a reported decision that was not brought to the attention of the Court to appreciate that the performance bond under consideration in *Larkin General Hospital* also expressly incorporated the underlying construction contract. Indeed, the terms of the performance bond in *Larkin General Hospital* not only incorporated the contract, but are almost exactly the same as the terms of the performance bonds in the instant case.

The opinion in *Larkin General Hospital* did not expressly set forth the terms of the performance bond. However, the Court did state that "[t]he language of the performance bond in the case at bar is identical to the language in the performance bond in *Arbor Club, Inc. v. Omega Constr. Co.*, 565 So. 2d 357 (Fla. 4th DCA 1990)." *Larkin General Hospital*, 593 So. 2d at 197. The Fourth District opinion in *Arbor Club* did set forth terms of that performance bond, specifically stating that "[t]he bond also provides that the contract between Omega and Arbor 'is by reference made a part hereof.'" *Arbor Club*, 565 So. 2d at 359. Thus, it is apparent that the performance bond in *Larkin General Hospital*, having language that is identical to the performance bond in *Arbor Club* that incorporated the contract, also incorporated the contract. Thus, the basis for distinguishing *Larkin General Hospital* in the Opinion is incorrect.

III. Once the Incorrect Distinction of *Larkin General Hospital* is Removed, it is Apparent that the Florida Supreme Court Rejected the Incorporation Analysis Applied by the Instant Opinion.

Larkin General Hospital reached the Florida Supreme Court based upon a certification of conflict between *Arbor Club of Boca Raton, Inc. v. Omega Constr. Co.*, 565 So. 2d 357 (Fla. 4th DCA 1990) and *United States Fidelity & Guar. Co. v. Gulf Florida Dev. Corp.*, 365 So. 2d 748 (Fla. 1st DCA 1978). As discussed above, the consideration in the Opinion of whether National Fire had any equitable subrogation rights under the performance bond unfortunately led to an incorrect means of distinguishing *Larkin General Hospital.* To compound that error, the Opinion uses the same analysis and reaches the same conclusion as in *Arbor Club.* This interpretation and holding was expressly rejected in *Larkin General Hospital.* In other words, without the benefit of briefs on this issue, and due to the mistaken distinction that the bond in *Larkin General Hospital* did not incorporate the contract, the Opinion erroneously reached the same interpretation and holding that was previously rejected by the Florida Supreme Court. Moreover, in a case that was apparently not considered by the Opinion on this point, the Florida Supreme Court recently expressly reaffirmed that *Larkin General Hospital* should be interpreted as rejecting the incorporation analysis adopted by the Opinion. *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998).

Arbor Club, Gulf Florida, Larkin General Hospital and the instant case all involved performance bonds that

incorporated the underlying contracts, but did not specify on their face that the surety was responsible for delay damages. The basis of the holding in *Arbor Club* was that "the bond incorporated the construction contract by reference, and that contract provided for timely performance." *Arbor Club*, 565 So. 2d at 360. Thus, the *Arbor Club* court held the performance bond surety liable for delay damages. In conflict with *Arbor Club*, the First District in *Gulf Florida*, faced with the same language in another performance bond, concluded that the terms of the performance bond limited the liability of the surety to the costs of completion and the costs of curing defective work. *Larkin General Hospital*, 593 So. 2d at 197. The Florida Supreme Court expressly adopted the holding of *Gulf Florida* and rejected the incorporation analysis of *Arbor Club*:

> The court in *Arbor Club* failed to construe the language in the performance bond in harmony with the subject matter of the bond and with the purpose of the bond. The purpose of a performance bond is to guarantee the completion of the contract upon default by the contractor. Ordinarily a performance bond only ensures the completion of the contract. The surety agrees to complete the construction or to pay the obligee the reasonable costs of completion if the contractor defaults.
>
> The liability of a surety is coextensive with that of the principal. However, the surety's liability for damages is limited by the terms of the bond. Florida courts have long recognized that the

> liability of a surety should not be extended by implication beyond the terms of the contract; i.e., the performance bond.
>
> We agree with the holding in *Gulf Florida* and with the court's interpretation of the performance bond language. Accordingly, we reject the holding and interpretation of the performance bond language in *Arbor Club* and *Wolley/Sweeney*. The terms of the performance bond control the liability of American [the surety]. The language in the performance bond, construed together with the purpose of the bond, clearly explains that the performance bond merely guaranteed the completion of the construction contract and nothing more. Upon default, the terms of the performance bond required American to step in and either complete construction or pay Larkin the reasonable costs of completion. Because the terms of the performance bond control the liability of the surety, American's liability will not be extended beyond the terms of the performance bond. Therefore, American cannot be held liable for delay damages.

Larkin General Hospital, 593 So. 2d at 198 (internal cites omitted). When the above holding is read with the understanding that the performance bonds in *Larkin General Hospital*, *Arbor Club*, *Gulf Florida*, and the instant case all incorporated the underlying construction contracts, it is apparent that the instant Opinion has misinterpreted *Larkin General Hospital*.

IV. The Florida Supreme Court Recently Confirmed that *Larkin General Hospital* Should be Interpreted to Reject the Incorporation Analysis. Additional Recent Case-Law, Published After the Submission of Briefs, Concurs in Interpreting *Larkin General Hospital* and Florida Law to Reject the Incorporation Analysis.

The Florida Supreme Court recently expressly reaffirmed that the proper interpretation of *Larkin General Hospital* is that the liability of a performance bond surety may not be extended by "contractual incorporation." *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998). Specifically, the Court adopted the reasoning of the lower court's dissent and held that the "incorporation" analysis improperly "extends the liability on the bond by implication beyond the terms of the bond contract. This additional burden is in derogation of the analysis provided by *Larkin General Hospital*." *Id.* at 1120-1121. Thus, following *Southwest Florida*, it is beyond doubt that the Florida Supreme Court does not agree with the "incorporation" analysis relied upon in the instant Opinion.

The most recent reported decision to interpret *Larkin General Hospital* is *Auto Owners Insurance Company v. Travelers Casualty & Surety Co.*, 227 F.Supp.2d 1248 (M.D. Fla. 2002). As this decision is dated September 12, 2002, after the submission of briefs in this case, it presumably was not considered by the Court. The Middle District undertook an extensive evaluation and discussion of both *Larkin General Hospital* and the subsequent Supreme Court opinion in *Southwest Florida Retirement*. *Auto Owners*, 227 F.Supp.2d at 1264-1265. The *Auto Owners* opinion explains

that in *Southwest Florida Retirement*, the Florida Supreme Court expressly "rejected the owner's argument that a surety's liability is co-extensive with the general contractor based on incorporation of the general contract into the performance bond." *Id.* at 1265. Similarly, the *Auto Owners* court found that "[a] holding that the incorporation provision may enlarge a surety's obligation under a bond, for both costs to complete a project and for damages that result from the project, would seem contrary to *Larkin*." *Id. Auto Owners* is simply one more example of established Florida law — a surety's liability is not extended by incorporation of the subcontract into the bond. The Opinion is contrary to that established principle.

CONCLUSION

The irony of this request for reconsideration is that granting it and correcting the obvious factual error in the Opinion regarding the interpretation of *Larkin General Hospital* will not vary the monetary result. However, the Opinion's favorable consideration of the incorporation argument rejected by the Florida Supreme Court in *Larkin General Hospital* can only serve to confuse an aspect of the law of suretyship in Florida which is now clear. Since *Larkin General Hospital*, owners, sureties and contractors have understood the rights and responsibilities they were undertaking in relation to consequential damages on bonded projects. That understanding leads to the clarity required to make intelligent business decisions. The Opinion will undermine that ability.

National Fire respectfully requests that the Court revisit the opinion and grant reconsideration on the points raised above.

* * * *

APPENDIX B — ANSWER AND AFFIRMATIVE DEFENSES OF FORTUNE CONSTRUCTION CO. DATED AUGUST 20, 1997 FILED IN THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF FLORIDA

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

CASE NO: 97-2439 CIV-KING

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, a Connecticut corporation,

Plaintiff,

vs.

FORTUNE CONSTRUCTION COMPANY, a Florida corporation,

Defendant.

ANSWER AND AFFIRMATIVE DEFENSES

Defendant, FORTUNE CONSTRUCTION COMPANY (hereinafter "FORTUNE"), files this Answer to the Complaint of Plaintiff, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD (hereinafter "NATIONAL FIRE"), and says:

1. As and for its answer to Paragraph 1, the same is admitted.

2. As and for its answer to Paragraph 2, the same is admitted.

Appendix B

3. As and for its answer to Paragraph 3, FORTUNE is without knowledge of the same and, therefore, denies the same and demands strict proof thereof.

COUNT I

4. As and for its answer to Paragraph 4, FORTUNE is without knowledge of the allegations contained therein and, therefore, denies the same and demands strict proof thereof.

5. As and for its answer to Paragraph 5, FORTUNE admits that NATIONAL FIRE issued bonds wherein FORTUNE was the obligee. In addition, FORTUNE admits it was the general contractor upon the projects known as West Brickell Apartments and Tract "G" at Winston Park, Coconut Creek, Florida. However, the bonds attached are not true copies of the originals of the same and, therefore, the remaining allegations of Paragraph 5 are denied.

6. FORTUNE admits that Arkin Construction Company, Inc. defaulted on the projects for which the bonds were issued by NATIONAL FIRE, but denies the remaining allegations contained in Paragraph 6.

7. As and for its answer to Paragraphs 7 and 8, the same are denied.

COUNT II

8. As and for its answer to Paragraph 9, FORTUNE realleges and reavers its previous responses to Paragraphs 1 through 3.

9. As and for its answer to Paragraph 10, FORTUNE is without knowledge of the allegations contained therein and, therefore, denies the same and demands strict proof thereof.

10. As and for its answer to Paragraph 11, the same is denied.

AFFIRMATIVE DEFENSES

That as and for its further Answer and Affirmative Defenses, Defendant, FORTUNE, says:

1. All allegations not specifically admitted herein are denied.

2. As reflected in the Complaint filed herein, Arkin Construction Company, Inc., the principal upon the bond, defaulted under the terms of its subcontract agreement. By virtue of said default and otherwise, FORTUNE has incurred damages and other expenses, including cost of completion, to the extent that there are no contract sums due to Arkin Construction Company, Inc. and, in fact, damages are due from Arkin Construction Company, Inc. to FORTUNE.

3. Upon the default of Arkin Construction Company, Inc. as set forth in the Complaint, demand was made upon Plaintiff, NATIONAL FIRE, to honor its bond obligations with regard to the Payment and Performance Bonds executed and delivered to FORTUNE with regard to the subject projects. NATIONAL FIRE failed and/or refused to so honor said obligations, thereby breaching the terms of its bonds.

NATIONAL FIRE is responsible to FORTUNE for damages incurred by FORTUNE arising from the default of Arkin Construction Company, Inc. and the default of NATIONAL FIRE, which damages are in excess of any contract balances at issue herein.

4. FORTUNE incorporates herein the allegations of its Counterclaim hereinafter set forth and further says that by virtue of the actions set forth therein, NATIONAL FIRE should be barred or is estopped to assert any claims against FORTUNE.

5. The actions of Plaintiff, NATIONAL FIRE, upon notice of default and demand for performance were such as to constitute bad faith and, as a result of the same, NATIONAL FIRE should be barred or estopped from any claim in this matter.

6. The actions of Plaintiff, NATIONAL FIRE, with regard to the projects in question constitute actions taken with unclean hands, thereby barring or estopping any claims herein.

7. As a result of the actions of NATIONAL FIRE, FORTUNE has been required to employ the undersigned attorneys to represent them in this matter and is entitled to attorney's fees in the defense of this action.

WHEREFORE, having fully answered the Complaint of Plaintiff, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, Defendant, FORTUNE CONSTRUCTION COMPANY, prays that the Court enter Judgment in its favor

and against Plaintiff and grant to Defendant, FORTUNE CONSTRUCTION COMPANY, all costs, expenses, and reasonable attorney's fees incurred in the defense hereof.

COUNTERCLAIM

Counterclaimant, FORTUNE CONSTRUCTION, INC. (hereinafter "FORTUNE"), files this Counterclaim against Counterdefendant, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD (hereinafter "NATIONAL FIRE"), and joins as an additional Counterdefendant, ARKIN CONSTRUCTION COMPANY, INC. (hereinafter "ARKIN"), and says:

1. This is an action for damages in excess of $15,000.

2. Counterclaimant, FORTUNE, is a Florida corporation with its principal office located in Dade County, Florida.

3. Counterdefendant, ARKIN, is a Florida corporation with its principal office located in Dade County, Florida.

4. Counterdefendant, NATIONAL FIRE is a Connecticut corporation authorized to issue surety bonds in the State of Florida.

COUNT I

5. On or about February 21, 1996, Counterclaimant, FORTUNE, and Counterdefendant, ARKIN, entered into a contract for the construction of a project described as Tract "G" at Winston Park, Coconut Creek, Florida. A true copy of said contract is attached hereto as Exhibit "A".

6. In connection with and conditioned to the performance of said contract, Counterdefendants, NATIONAL FIRE, as surety, and ARKIN, as principal, did execute and deliver to Counterclaimant a Performance Bond wherein FORTUNE was the named obligee. A true copy of the Performance Bond, including a Dual Obligee Rider, is attached hereto as Composite Exhibit "B".

7. ARKIN commenced construction of the project and continued with the same until abandoning the project on or about May 29, 1997.

8. Thereafter, Counterclaimant, FORTUNE, declared ARKIN in default of its contract obligations and notified NATIONAL FIRE of the same.

9. In addition, FORTUNE demanded that NATIONAL FIRE honor its obligations under the Performance Bond attached hereto as Exhibit "B".

10. Despite said demands, NATIONAL FIRE has failed and refused to honor its obligations under the aforesaid surety bond and has breached not only its obligation to remedy the default of its principal, ARKIN, but also its obligation to perform those duties set forth in the bond as surety.

11. By virtue of the aforesaid default by ARKIN, as well as the breach of the obligations under the Performance Bond by NATIONAL FIRE, Counterclaimant has been damaged.

12. The damages incurred by Counterclaimant are in excess of $15,000 and include, but are not limited to, the

following which may encompass consequential and/or special damages contemplated by the parties:

(a) Direct and indirect project completion costs;

(b) Payments to subcontractors, laborers, and materialmen;

(c) Increased overhead and administrative expenses;

(d) Interest expenses;

(e) Impact to other projects, including interest and delay expenses;

(f) Lost opportunity to undertake other projects;

(g) Lost profits;

(h) Delay damages caused by the failure of the surety to perform its obligations; and

(i) Contractual damages due from FORTUNE to owner.

13. All conditions precedent to this action have been performed, have occurred, or have been waived.

14. As a result of the actions of Counterdefendant, NATIONAL FIRE, Counterclaimant has been required to

employ the services of the undersigned counsel to represent it in this matter and has agreed to pay a reasonable fee for their services.

WHEREFORE, Counterclaimant, FORTUNE CONSTRUCTION, INC., prays that the Court enter Judgment against Counterdefendants, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD and ARKIN CONSTRUCTION COMPANY, INC., for all damages incurred, including those consequential and special damages listed above, together with interest, costs, and reasonable attorney's fees.

COUNT II

15. Counterclaimant realleges and reavers Paragraphs 1 through 4 as if more fully set forth herein.

16. On or about January 15, 1996, FORTUNE and Counterdefendant, ARKIN, entered into a contract for the construction of a project known as West Brickell — 130 Apartments — Miami, Florida. A true copy of said contract is attached hereto as Exhibit "C".

17. In connection with and conditioned to the performance of said contract, Counterdefendants, NATIONAL FIRE, as surety, and ARKIN, as principal, did execute and deliver to Counterclaimant a Performance Bond wherein FORTUNE was the named obligee. A true copy of the Performance Bond is attached hereto as Exhibit "D".

Appendix B

18. ARKIN commenced construction of the project and continued with the same until abandoning the project on or about May 29, 1997.

19. Thereafter, Counterclaimant, FORTUNE, declared ARKIN in default of its contract obligations and notified NATIONAL FIRE of the same.

20. In addition, FORTUNE demanded that NATIONAL FIRE honor its obligations under the Performance Bond attached hereto as Exhibit "D".

21. Despite said demands, NATIONAL FIRE has failed and refused to honor its obligations under the aforesaid surety bond and has breached not only its obligation to remedy the default of its principal, ARKIN, but also its obligation to perform those duties set forth in the bond as surety.

22. By virtue of the aforesaid default by ARKIN, as well as the breach of the obligations under the Performance Bond by NATIONAL FIRE, Counterclaimant has been damaged.

23. The damages incurred by Counterclaimant are in excess of $15,000 and include, but are not limited to, the following which may encompass consequential and/or special damages contemplated by the parties:

(a) Direct and indirect project completion costs;

(b) Payments to subcontractors, laborers, and materialmen;

Appendix B

(c) Increased overhead and administrative expenses;

(d) Interest expenses;

(e) Impact to other projects, including interest and delay expenses;

(f) Lost opportunity to undertake other projects;

(g) Lost profits;

(h) Damages caused by the failure of the surety to timely and properly perform its obligations;

(i) Rental loss;

(j) Additional marketing expenses;

(k) Finance penalties;

(l) Loss of reputation; and

(m) Contractual damages due from FORTUNE to owner.

24. All conditions precedent to this action have been performed, have occurred, or have been waived.

25. As a result of the actions of Counterdefendant, NATIONAL FIRE, Counterclaimant has been required to

employ the services of the undersigned counsel to represent it in this matter and has agreed to pay a reasonable fee for their services.

WHEREFORE, Counterclaimant, FORTUNE CONSTRUCTION, INC., prays that the Court enter Judgment against Counterdefendants, ARKIN CONSTRUCTION COMPANY, INC. and NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, for all damages incurred, including those consequential and special damages listed above, together with interest, costs, and reasonable attorney's fees.

* * * *

Supreme Court, U.S.
FILED
AUG 18 2003
OFFICE OF THE CLERK

No. 03-12

In the

Supreme Court of the United States

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD,

Petitioner,

v.

FORTUNE CONSTRUCTION COMPANY,

Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

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I. FORTUNE'S ARGUMENT THAT NO CONFLICT IS PRESENTED IS ABSURD.

Fortune's contention that no conflict is presented between the Eleventh Circuit's subject opinion, the Fifth Circuit's opinion in *L & A Contracting Co. v. Southern Concrete Services*, 17 F.3d 106 (5th Cir. 1994), and the Florida Supreme Court's opinion in *American Home Assurance Co. v. Larkin General Hospital*, 593 So. 2d 195 (Fla. 1992) is nonsensical and strains good faith. Fortune does not dispute that *Larkin* holds "that a performance bond surety is not liable for delay damages unless the bond specifically provides coverage for delay damages." *Larkin*, 593 So. 2d at 196. The Eleventh Circuit distinguished *Larkin* because, "unlike the performance bond in *Larkin*, the bonds at issue in this case expressly incorporated the subcontracts." (Appendix, p. 22). As discussed more fully in National Fire's Petition for a Writ of Certiorari, this is just wrong. The bond in *Larkin* contained the exact same form language incorporating the construction contracts as the bonds in this case.[1]

Fortune does not dispute that the only basis asserted by the Eleventh Circuit to distinguish *Larkin* is incorrect. Instead, Fortune concocted a new theory that *Larkin* and *L & A* may be distinguished because the construction contracts in *Larkin* and *L & A* did not contain provisions that established a liquidated daily rate of damages in the event of untimely completion by

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[1] *Larkin* states that "[t]he language of the performance bond in the case at bar is identical to the language in the performance bond in *Arbor Club, Inc. v. Omega Constr. Co.*, 565 So. 2d 357 (Fla. 4th DCA 1990) and *Gulf_Florida*." *Larkin*, 593 So. 2d at 197. The opinion in *Arbor Club* set forth the text of the bond in full, and it is the same as the bond language in the instant case. *Arbor Club*, 565 So. 2d at 359. The *Arbor Club* opinion made note that the bond incorporated the contracts.

the contractor. (Brief in Opposition, pp. 11-12). As discussed below, the opinions do not suggest this is true.

More importantly, this argument is so devoid of wisdom or good sense as to be laughable. It is not sensible to say that *liability* for delay damages could turn upon whether the contractor and owner agreed in advance to the *measure of damages* for delay. A liquidated damages provision may provide a means to measure quantum of delay damages, but it is meaningless to establish the occasions when such delay damages are applicable. *U.S. v. American Surety Co.*, 322 U.S. 96, 99 (1944) ("A provision in a public construction contract fixing a certain amount as liquidated damages for each day's delay merely served to provide the agreed rate of damages to be paid if liquidated damages were required to be paid under the contract, and could not have effect of spelling out situations where such damages were to be paid."). Regardless of whether a construction contract contains a liquidated delay damages provision, the contractor is always liable for delay damages if it fails to timely complete its work; a liquidated delay damages provision is merely an advance agreement as to the quantum of those damages. *Hartford Fire Ins. Co. v. Controltec, Inc.*, 561 So. 2d 1334 (Fla. 5th DCA 1990). It is absurd to contend, as Fortune does, that a surety is liable for delay damages if the contractor and owner agree upon their measurement by using a liquidated delay damages provision, but that the surety is not liable for the same damages if the contractor and owner do not so agree, and the owner is left to prove its actual damages.

Fortune repeatedly and brazenly asserts that the underlying construction contracts in *Larkin* and *L & A* did not contain provisions liquidating the amount of damages in the event of a delay in completion by the contractor. (Brief in Opposition, pp. 10-12). The

opinions do not suggest this to be true.[2] In *Larkin*, the contractor failed to complete its work by the contracted completion date and the owner terminated the contract. *Larkin*, 593 So.2d at 196. The owner sued the contractor and surety for delay damages attributable to the contractor's untimely performance. *Id.* The opinion does not mention whether the measurement of delay damages was based upon a liquidated damages provision – but there is no suggestion that this is a relevant inquiry. Rather, the issue was *liability* ("whether a surety on a performance bond can be held liable for consequential delay damages caused by the contractor's default") rather then the measurement of the delay damages (which is the only purpose of a liquidated delay damages provision). *Id.* at 196.

Moreover, *Larkin* was considered by the Court because of conflict between *Arbor Club of Boca Raton v. Omega Construction Co.*, 565 So. 2d 357 (Fla. 4th DCA 1990) and *USF&G Co. v. Gulf Florida Development Corp.*, 365 So. 2d 748 (Fla. 1st DCA 1979). In both cases, the bond incorporated the underlying contract, and the contractor was liable for delay damages; at issue was whether the surety was also liable. *See*, *Arbor Club*, 565 So. 2d at 358-360; *Gulf Florida*, 365 So. 2d at 749-750. Neither opinion made any mention as to whether the measurement of delay damages was liquidated, further disabusing Fortune's argument that the presence of a liquidated damages clause can be the "pivotal fact" for determining the liability of the surety. (Brief in Opposition, p. 3).

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[2]The bonds under consideration in both *Larkin* and *L & A* incorporated the underlying contracts; the respective contractors were liable for substantial delay damages. *Larkin*, 593 So. 2d at 197 and *L & A*, 17 F.3d at 109. The sureties were held to not be liable for delay damages, because such liability was not included in the "express terms of the bond." *L & A*, 17 F.3d at 112 (interpreting *Larkin*).

Similarly, *L & A* involved a contractor that sued its subcontractor and its subcontractor's surety for damages arising from the subcontractor's tardy performance. *L & A*, 17 F.3d at 108. The opinion does not express whether the quantum of the delay damages was measured by the contractor proving its actual damages, or a liquidated damages provision. However, it is apparent from the Court's analysis that the question of whether the amount of damages was measured by a liquidated damages provision is not relevant.[3] Not only

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[3]This was expressed by the Fifth Circuit as follows:

> [The surety] next challenges the district court's judgment holding it liable for delay damages. We need not linger long on this question because it is directly controlled by the Florida Supreme Court's opinion in *Larkin*. The *Larkin* Court held that "the surety's liability for damages is limited by the terms of the bond". The bond here contained no provision imposing liability upon [the surety] for delay damages, and the district court may not imply such a provision. Therefore, the district court erred in holding [the surety] liable for delay damages. We are not persuaded by [the general contractor]'s attempts to distinguish away the clear command of *Larkin*.
>
> [General contractor] first contends that the bond in *Larkin* contained different language from [the surety]'s bond. Even if that is true – and [the surety] contends that it is not – it is irrelevant. *Larkin* did not turn on the language of the particular bond before the Court in that case, but rather stated what was obviously intended to be a general proposition of law. Second, [the general contractor] contends that [the surety's] bond was ambiguous, but even if it were, that is irrelevant to this issue. *Larkin* plainly states that the express terms of the bond provide the sole measure of [the surety's] obligation. If [the surety]'s liability for delay damages is not "*expressed in the bond*", *Id.* at 198 (emphasis added by Fifth Circuit), [the surety] has no such liability.

do *Larkin* and *L & A* not suggest that the contracts failed to include liquidated delay damages provisions, but they also demonstrate that such provisions has no relevance to determining the liability of the surety. Thus, the Court should not give credence to Fortune's contention that no conflict exists.

II. FORTUNE'S ARGUMENT THAT THE SUBJECT DECISION HAS NO NEW RAMIFICATIONS FOR THE SURETY INDUSTRY SAYS NOTHING.

Fortune makes three contentions in section II of its Brief. The first is that sureties are not required to use form bonds. (Brief in Opposition, p. 12). This is true, but is no comfort to the surety industry with regard to the multitude of presently outstanding bonds issued under the belief and intention that this bond language does not include liability for delay damages.[4] Fortune's second contention is "the fact that some performance bonds are held to cover actual and liquidated delay damages has long been known to the surety industry." (Brief in Opposition, p. 12). This is true, but the bond under consideration was declared by the Florida Supreme Court to not cover delay damages. *Larkin*, 593 So. 2d at 196.[5] Similarly, Fortune's third contention is that there is no "novelty to the fact that the delay damage liability may be triggered by language in a bond incorporating by reference the terms of an underlying construction contract." (Brief in Opposition, p. 14). In fact, this is entirely novel *in Florida* after *Larkin*.

Id. at 112.

[4]The language at issue is the most commonly used bond form. 3 *Bruner & O'Connor Construction Law* §8:156 (2003).

[5]Fortune cites nine cases interpreting various bonds in a variety of jurisdictions. *Larkin* similarly recognized the inconsistency in other jurisdictions and sought to establish a definitive interpretation. *Larkin*, 593 So. 2d at 197-198.

III. FORTUNE'S ALLEGED "MISSTATEMENTS IN THE PETITION" IS THE POT CALLING THE KETTLE BLACK.

A. Fortune's Allegations that National Fire has Misrepresented Facts is itself a Misrepresentation.

Throughout this litigation, National Fire has only had respect for Fortune's counsel and does not believe they would purposefully mislead the Court. Therefore, National Fire suspects that the attorneys involved in the District Court action are not the authors of its Brief. Anyone associated with the District Court action knows that Fortune only asserted its liquidated damages claim in the framework of a "set-off" that could be applied to Arkin's (the contractor) unpaid contract balances, rather than an affirmative claim for recovery under the performance bonds.[6]

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[6]For example, in *Fortune's Supplemental Memorandum of Law in Reply to National Fire's Motions for Partial Summary Judgment*, Fortune specifically asserted that its theory of recovery was only as a "set-off" and explained that it was not seeking an affirmative recovery. Specifically, Fortune stated as follows:

> National Fire has attempted to confuse the issues before this Court by raising the question of the assessment of liquidated damages against the surety for the breach of the principal [the circumstance addressed by *Larkin*]. This is not the question which will be faced by the Court. The real issue is the appropriateness of the assessment of liquidated damages pursuant to the terms of the subcontracts against the Arkin Contract balances. As demonstrated by the filings previously made herein, with regard to the Winston Park project, in excess of $1.6 million in liquidated damages have accrued and have been assessed against the contract balances.
>
> * * *
>
> As a result, Fortune has done nothing other than assess against Arkin, and the Arkin subcontracts, those amounts which have been

The goal of this approach was to avoid *Larkin* by contending that although that case barred recovery of delay damages against the surety, Fortune may still apply its liquidated delay damage claim to reduce the contract balances that would otherwise be paid to the surety. Fortune argued that it had already applied the liquidated delay damages "assessment" against the contractor. Since it claimed to have already been so compensated, it would have been factually inconsistent for Fortune to also seek affirmative recovery of the same liquidated delay damages against National Fire; and such a recovery was barred by *Larkin* anyway.

Consistent with this approach, Fortune pled the set-off of the liquidated delay damages as an affirmative defense, but did not pursue an affirmative claim for the delay damages. (Respondent's Appendix, pp. 16a-18a). Specifically, only two types of "delay damages" are sought in the Counterclaim. *Id.* First, subparagraph 12(2) sought recovery of "[i]mpact to other projects, including interest and delay expenses." *Id.* In this subparagraph, Fortune sought recovery of <u>impacts to other projects</u>, not liquidated delay damages on the bonded projects. Second, subparagraph 12(h) sought recovery of "delay damages caused by the failure of the

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> incurred and are properly chargeable under the terms of the subcontracts.
>
> The surety has attempted to deviate from the real issue by asserting that it is being charged with "delay damages", for which it contends a surety may not be liable under Florida law [the affirmative claim of *Larkin*]. However, the cases cited by the surety do <u>not</u> address the situation in which sums are charged against contract balances as liquidated damages nor, for that matter, address in any way the assessment of contractual damages against contract proceeds.

(Reply Brief Appendix, pp. 4a-5a).

surety to perform its obligations." *Id.* This allegation sought recovery of delay damages allegedly arising from National Fire's post-default failure to satisfy its alleged obligation to complete Arkin's projects in a timelier manner than they actually were completed – it does not refer to liquidated delay damages that arose prior to the default of the contractor.

As discussed in National Fire's Petition, the Eleventh Circuit did not appreciate this nuance and mistakenly believed that Fortune sought to recover the liquidated damages from National Fire as an affirmative claim. (Petition, p. 5-6). The Eleventh Circuit's opinion is largely devoted to a misunderstanding of the record, and prior to issuing its opinion, it did not have the benefit of briefs on such issues, which were not before it. *Id.* The author of Fortune's Brief apparently did not review the underlying record or discuss this nuance with the attorneys that represented Fortune in the District Court action, as the Brief incorrectly accuses National Fire of misrepresenting this issue. (Brief in Opposition pp. 16-19). Specifically, Fortune contends, with much bluster, that its Counterclaim did contain an affirmative claim that was pursued in the District Court. *Id.* Despite the bluster, this is just wrong.

Lastly, National Fire's Petition explained that the Eleventh Circuit only addressed the question presented because it misunderstood the record. (Petition, pp. 4-7).[7]

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[7]Specifically, the Eleventh Circuit mistakenly believed that National Fire sought to assert equitable subrogation rights arising from the performance bonds, rather than the payment bonds, and held that the District Court erred by granting National Fire summary judgment on equitable subrogation arising out of the performance bonds. *Id.* However, National Fire made no such claim, nor would there be any basis for such a claim, and no such summary judgment was made or granted. *Id.* Similarly, as discussed in the previous section, the Eleventh Circuit mistakenly believed that Fortune sought to recover the liquidated delay damages from National Fire in the underlying suit under a theory

Therefore, it issued an opinion demonstrating a misunderstanding of the record, National Fire petitioned for reconsideration. The Eleventh Circuit denied this petition. (Appendix, p. 43). Fortune relies upon this petition for reconsideration for its misstatement that "it is inaccurate for Petitioner to state that the Eleventh Circuit was never given any briefing on these issues that the Petitioner claims the Eleventh Circuit misunderstood." (Brief in Opposition, p. 15). However, National Fire did not express that the Eleventh Circuit "was never given any briefing," rather, National Fire correctly pointed out that the opinion is largely devoted to matters that were not the subject of the briefs submitted, as the opinion is based upon a misunderstanding of the record. (*See*, Brief in Opposition, p. 15).

B. Fortune's Allegations that National Fire has Misrepresented Case law is itself a Misrepresentation.

Fortune's Brief repeatedly places an untenable interpretation upon *Larkin* and *L & A*. National Fire stands by its statement that "[u]nder the holding of these cases, if a performance bond specifies that it incorporates the underlying contract, but it does not specify on its face that the surety is responsible for delay damages arising from untimely performance of the underlying contract, liability for delay damages is not imposed upon the surety." (Petition, p. 6). Fortune claims this "is clearly a misrepresentation of the holdings of these cases. . . Neither decision says that liability for delay damages will not be imposed upon a surety whose bond incorporates a delay damage

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that they were a responsibility of National Fire under the performance bonds. Accordingly, the briefs before the Eleventh Circuit did not address these nonexistent claims or the nonexistent summary judgment order.

provision by reference rather than stating it on the face of the bond." (Brief in Opposition, p. 16). Actually, that is exactly what these cases hold.[8]

Finally, the Florida Supreme Court reaffirmed that the proper interpretation of *Larkin* is that the liability of a surety may not be extended by "contractual incorporation" in *Federal Insurance Co. v. Southwest Florida Retirement Center, Inc.*, 707 So. 2d 1119 (Fla. 1998), another case Fortune contends National Fire misrepresents. (Brief in Opposition, p. 15). The *Southwest Florida* opinion specifically held that the "incorporation" analysis (championed by Fortune) improperly "extends the liability on the bond by implication beyond the terms of the bond contract. This additional burden is in derogation of the analysis provided by *Larkin*." *Id.* at 1120-1121. Thus, following *Southwest Florida*, it is beyond doubt that Fortune's interpretation of *Larkin* is wrong, and National Fire has not misrepresented either opinion.

IV. CONCLUSION.

National Fire again submits that this is an exceptional case, warranting the grace of a grant of certiorari, and requests that its petition be granted.

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[8] *Larkin*, 593 So. 2d at 196 ("We hold that a surety cannot be held liable for delay damages due to the contractor's default unless the bond specifically provides coverage for delay damages. . . . The surety's liability for damages is limited by the terms of the bond. Florida courts have long recognized that the liability of a surety should not be extended by implication beyond the terms of the contract, i.e., the performance bond.); *L & A*, 17 F.3d at 198 ("*Larkin* plainly states that the express terms of the bond provide the sole measure of [the surety's] obligation. If [the surety]'s liability for delay damages is not "*expressed in the bond*", [the surety] has no such liability.").

CASE NO. 97-2439 CIV-KING

UNITED STATES DISTRICT COURT SOUTHERN DISTRICT OF FLORIDA MIAMI DIVISION

NATIONAL FIRE INSURANCE COMPANY OF HARTFORD, a Connecticut corporation,
Plaintiff,

vs.

FORTUNE CONSTRUCTION COMPANY, a Florida corporation, Defendant,

vs.

ARKIN CONSTRUCTION COMPANY, INC.,
Third-Party Defendant.

FORTUNE CONSTRUCTION COMPANY'S SUPPLEMENTAL REPLY TO PILAINTIFF'S MOTIONS FOR SUMMARY JUDGMENT

Defendant/Counterclaimant, FORTUNE CONSTRUCTION COMPANY (hereinafter "FORTUNE"), files this Supplemental Reply to Plaintiff /Counterdefendant's, NATIONAL FIRE INSURANCE COMPANY OF HARTFORD (hereinafter "NATIONAL FIRE"), Motions for Partial Summary Judgment and says:

SUPPLEMENT TO:

II. SURETY FAILED TO PERFORM THE OBLIGATIONS ENUMERATED TINDER THE BOND

As to the argument of NATIONAL FIRE concerning the "tender" of a completion contractor, and in further

support of FORTUNE'S argument, the deposition testimony taken herein is at variance with the representations made and assertions made within the motion.

NATIONAL FIRE has asserted and represented that it "tendered" a completion contractor to FORTUNE. (See Secpnd Motign for Partial Summary Judgment, Page S, Paragraph 22) Further, NATIONAL FIRE has represented that it had no responsibility to make such a tender. This assertion as to the Winston Park project ignores the clear requirements of the obligation of NATIONAL FIRE to FORTUNE in the performance bond which requires the surety to:

"(1) Complete the contract . . . or

(2) Obtain a bid or bids for completing the contract and arrange for a contract between such bidder and the owner. . ." (Complaint, Exhibit 2) (emphasis added)

The second obligation referenced above allows the surety to "tender" a completion contractor to work directly for the owner (FORTUNE). However, despite the representations of NATIONAL FIRE, the depositions have reflected that no such tender occurred, and that the alleged "completion contractor" was unwilling to contract directly with the "owner" (FORTUNE) or act as a completing contractor.
The deposition of J. Robert Stobs, II of Stobs Construction reflects the following:

"Q: You mentioned that you would be willing to perform the work under the right circumstances. Would you please go over the right circumstances for me, please?

A: That I would be working for the bonding company.

Q: Why was that important?
A: Because I didn't want to be responsible for the warranty or any part of that on a project that was already under construction by somebody else. I would not assume the liability for it . . .

Q: Did you understand that you would be the general contractor as opposed to a construction manager?
A: No, I did not know that.

Q: Was that -
A: That was not discussed.

Q: That was not discussed?
A: No . . ." (Page 13)

Q: "In as far as becoming the general contractor on the project, you were not willing to go that far? . . .
A: Again, we were not going to do anything that would put us in a warranty type situation with the owner.

Q: Would that be including the general contractor?
A: Again, we never discussed that as such. Being the contractor of record, is that what you are saying?

Q: Yes.
A: We never discussed that." (Page 15) (Attached hereto as Exhibit "A")

The above deposition testimony of the representative of the alleged "completion contractor" demonstrates that there was never any arrangement between the surety

and Stobs Brothers which would constitute a tender in accordance with the terms of the Winston Park performance bond.

Certainly, the deposition testimony is at variance with the Affidavit and representations submitted by the surety and call into ouestion the veracity of NATIONAL FIRE.

SUPPLEMENT TO:

III. OBLIGEE IS ENTITLED TO CONTRACT ADJUSTMENTS DERIVED FROM THE ORIGINAL OBLIGATION

3) Assessment of Liquidated Damages Against Contract Balances is Appropriate

NATIONAL FIRE has attempted to confuse the issues before this Court by raising the question of the assessment of liquidated damages against the surety for the breach of the principal. This is not the question which will be faced by the Court. The real issue is the appropriateness of the assessment of liquidated damages pursuant to the terms of the subcontracts against the ARKIN contract balances. As demonstrated by the filings previously made herein, with regard to the Winston Park project, in excess of $1.6 million in liquidated damages have accrued and have been assessed against the contract balances.
NATIONAL FIRE has recognized and agreed that ARKIN and ARKIN'S subcontracts are chargeable for liquidated damages incurred by FORTUNE. (See Lemming deposition, Page 56, Lines 6-10; Exhibit "B")

The damages asserted by FORTUNE and attached to the previous filings as Exhibits "A" to the Affidavits of

Michael Getz and Michael Spetko, respectively, reflect the assessment of liquidated damages against the subcontract sums "due ARKIN" or which would "come due to ARKIN under the subcontracts" had ARKIN completed the projects.

As a result, FORTUNE has done nothing other than assess against ARKIN, and the ARKIN subcontracts, those amounts which have been incurred and are properly chargeable under the terms of the subcontracts.

The surety has attempted to deviate from the real issue by asserting that it is being charged with "delay damages", for which it contends a surety may not be liable under Florida law. However, the cases cited by the surety do not address the situation in which sums are charged against contract balances as liquidated damages nor, for that matter, address in any way the assessment of contractual damages against contract proceeds.

Such a discussion occurred in the case of Pacific Employers Insurance Company vs. City of Berkley, 158 Cal.App.3d 145, 204 Cal.Rptr. 2387 (1984). In Pacific Employers, the surety actually completed a project upon which it had issued a performance bond. (In this case, the surety has not performed under its performance bond.) Upon completion of the project, the owner assessed liquidated damages against the contract balances and proffered the remainder to the surety. The surety contended that when it elected to complete the contract, it was entitled to the entire undisbursed contract funds and that the owner could not offset liquidated damages against those sums.

In rejecting this argument, the Court found two significant bases for permitting the reduction of the contract balances:

(1) By performance, the surety stayed in the same position to the contract as did the original contractor. As a result, the performing surety was subject to the contractor's obligations, which included liquidated damages.

(2) The Court held that the case came within the general rule that a party may offset monies owed under a contract by the amount of damages suffered.

The law in Florida is consistent with the holding of Pacific Employers, supra, with regard to the assessment of contractual offsets against contract balances. See Marriott Corporation vs. Dasta Construction Company, 26 F.3d 1057 (Fla. 11th Cir 1994) ; Ever Block & Ready Mix Company vs. Wheeler, 207 So.2d 698 (Fla. 3rd DCA 1968); Russo vs. Heil Construction, Inc.. 549 So.2d 676 (Fla. 5th DCA 1989).

In Marriott, supra, above, a contractor pursued claims for contract balances against an owner. However, the owner had been required to make payment to subcontractors and suppliers of the contractor to remove mechanic's liens on its projects in a sum in excess of the remaining contract balances. Pursuant to a contract term, the general contractor had agreed that the owner would be reimbursed for all such sums.
As a result, the Eleventh Circuit Court of Appeals held that the general contractor, being obligated to remove such claims and therefore breaching its contract provision, was not permitted recovery hut, rather, the owner was "entitled to setoff the entire remaining

amount of the outstanding contract balances". (Page 1071)

The situation before this court is identical. The contract provides for the assessment of liquidated damages for the failure to timely perform. By virtue of the failure of the contractor to timely perform, it is appropriate for liquidated damages to he assessed against the contract balances of the contractor under Florida law.

FORTUNE would again call the Court's attention to the provisions of the surety bonds and the definition of contract balances contained within that document, a form document of NATIONAL FIRE. With regard to that definition, the performance bond for the Winston Park project defines the balance of the contract price as:

"The total amount payable by the owner to contractor under the contract and any amendments thereto, less the amount properly paid by owner to contractor."

As to the West Brickell project, the language is identical with the exception that the term "subcontract" has been substituted for "contract".

By virtue of the specific delineation of the amounts due, and referencing them to the amounts due under the "contract", the contract balances as defined by the surety in the bonds must be reduced by those offsets provided for by the terms of the subcontracts, including the deduction of liquidated damages.

The position of NATIONAL FIRE is simply inequitable. By not performing under the performance bonds in this case, NATIONAL FIRE Contends that FORTUNE may not enforce the obligations of the very contract upon which its bonds are conditioned.

FORTUNE would respectfully urge that its causes of action asserted in this case are based upon the contract of ARKIN, the rights and liabilities under that contract, and the obligations of NATIONAL FIRE as defined by their bonds. The actions asserted by NATIONAL FIRE are based upon the obligations of ARKIN to FORTUNE and the alleged rights of ARKIN under its subcontracts with FORTUNE. (See Complaint)[1]

In supplement to its previous arguments, FORTUNE would additionally argue that by virtue of the above authority and argument, that the assessment of liquidated damages against contract balances is appropriate under the contracts bonded by the surety and the terms of the bonds.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing was mailed to Michael Piscitelli, Esq., VEZINA, LAWRENCE & PISCITELLI, P.A., Attorneys for Plaintiff, 500 East Broward Boulevard, Suite 1850, Ft. Lauderdale, FL 33394 and to L. Jules Arkin, Esq., Attorney for Third-Party Defendant, 8801 SW 68th Avenue, Miami, FL 33156 on this 2nd day of July, 1998.

WELBAUM, GUERNSEY, HINGSTON, GREENLEAF & GREGORY, L.L.P.
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(305) 441-8900

BY: ROBERT A. HINGSTON, ESQ.
Florida Bar No. 181185

FOOTNOTES

[1] NATIONAL FIRE'S Complaint is stated in two separate counts. The first count is a cause of action based upon an assignment of rights of ARKIN CONSTRUCTION COMPANY, INC. (hereinafter "ARKIN") under an alleged General Agreement of Indemnity attached to the Complaint as Exhibit "A". Clearly, under this theory, the surety steps into the shoes of its contractor, ARKIN, by contract and is asserting the claims of ARKIN for sums due.

Count II of the Complaint asserts rights of subrogation, again alleging rights to sums which are due to ARKIN or money which would become due to ARKIN under the subcontracts between ARKIN and FORTUNE. NATIONAL FIRE requests an Order "requiring FORTUNE to pay to NATIONAL FIRE all amounts due ARKIN and all amounts which will come due to ARKIN under the subcontracts".

CASE NO. 97-2439 CIV-KING

UNITED STATES DISTRICT COURT SOUTHERN DISTRICT OF FLORIDA MIAMI DIVISION

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Plaintiff,

vs.

FORTUNE CONSTRUCTION COMPANY, a Florida corporation, Defendant,

vs.

ARKIN CONSTRUCTION COMPANY, INC.,
Third-Party Defendant

Penthouse Suite
901 Ponce de Leon Boulevard
Coral Gables, Florida
Monday, 10:05 A.M.
April 6, 1998

DEPOSITION OF J. ROBERT STOBS. II

Taken by the Defendant, before JOE D. HAMMOND, a Court Reporter and Notary Public in and for the State of Florida at Large, pursuant to a Notice of Taking Deposition filed in the above cause.

Q. You have no idea when that call could have occurred?
A. No, T do not.

Q. You mentioned that you would be willing to perform the work under the right: circumstances. would you please go over the right circumstances for me, please?
A. That I would be working for the bonding company.

Q. Why was that important?
A. Because I didn't want to be responsible for the warranty or any part of than on a project that was already under construction by somebody else. I would not assume the liability for in.

Q. Why was chat a problem?
A. Because I don't know what has gone on in the past. I don't know the completion of the project, I don't know the subcontractors.

Q. Did you understand that you would be the general contractor as opposed no a construction manager?
A. No, I did not know that.

Q. Was that - -
A. Than was not discussed.

Q. That was not discussed?
A. No.

Q. Were you willing to perform the work as a management supervision, and I said yes, we would.

Q. In a6 far as becoming the general contractor on the project, you were not willing to go that far?

MR. PISCITELLI: I object to the form. You can answer. It was just vague.

THE WITNESS: Again, we were not going to do anything that would put us in a warranty type situation with the owner.

BY MR. HINGSTON:

Q. Would that be including the general contractor?
A. Again, we never discussed that as such. Being the contractor of record, is that what you are saying?

Q. Yes.
A. We never discussed that.

Q. Were you willing to perform that function?
A. I would have to have conversation to see what the responsibili-ties would have been.

Q. Other than working directly for the bonding company as a construction manager, what other circumstances would have had to have been fulfilled for you to enter into the contract with the bonding company?

MR. PISCITELLI: I object to the lack of predicate.

CASE NO. 97-2439 CIV-KING
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Plaintiff,

vs.

FORTUNE CONSTRUCTION COMPANY, a Florida corporation, Defendant,

vs.

ARKIN CONSTRUCTION COMPANY, INC.,
Third-Party Defendant

Penthouse Suite
901 Ponce de Leon Boulevard
Coral Gables, Florida
Thursday, 11:00 A.M.
March 19, 1998

DEPOSITION OF RAY LEMMING, ESQUIRE

Taken by the Defendant, before JOE D. HAMMOND, a Court Reporter and Notary Public in and for the State of Florida at Large, pursuant to a Notice of Taking Deposition filed in the above cause.

A. In the contract, but not as a liability to the surety.

Q. But there were liquidated damages in the contract?
A. Yes.

Q. Did you understand Arkin would be responsible for the Liquidated damages?
A. Yes.

Q. And be chargeable for those?
A. Yes.

Q. So, since we are talking about this meeting and we now have got a $750,00n offer from your company to Fortune under the terms that you set forth, did you come away from the meeting understanding the matter had been resolved in the event you could get $1,000,000?
A. That Winston had been resolved. We had tabled Brickell at that point. That is a partial yes, that anything on Winston would be resolved.

Q. But you had not yet got the $1,000,000 worth of authority?
A. No, not at that point.

Q. Your view is the other terms were acceptable to Fortune?
A. Correct, as I outlined them for you earlier in the deposition. They would assume the contracts and